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IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-6881

L Q MOTOR INNS, INC., SAMUEL E. BARSHOP, PHILIP M. BARSHOP, DORIS BARSHOP SPECTOR, AND NORMAN S. DAVIS

v.

BERNARD D. SPECTOR

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT.

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In The

Supreme Court of the United States

October Term, 1975

No. .....

L Q Motor Inns, Inc., Samuel E. Barshop,
Philip M. Barshop, Doris Barshop Spector,
and Norman S. Davis

v.

Bernard D. Spector

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT.

Petitioners pray that a Writ of Certiorari issue to review an opinion and order of the United States Court of Appeals for the Fifth Circuit reversing an order of the United States District Court for the Western District of Texas, which had granted Petitioners' Motion to Dismiss for Lack of Subject Matter Jurisdiction on the grounds that the transaction involved was part of an indivisible Texas divorce and property settlement, solely within the jurisdiction of the State Courts, and was not a "sale" within the meaning of the Securities Exchange Act of 1934, and SEC Rule 10b-5.

OPINIONS BELOW

The opinion of the Court of Appeals is officially reported at 517 F.2d 278 (5th Cir., 1975). It is set forth herein as Appendix A, *infra*, pp. 1a through 19a. The District Court's Memorandum Opinion dismissing Respondent's claim for lack of subject matter jurisdiction, dated May 7, 1974, is set forth herein as Appendix B, *infra*, pp. 20a through 22a.

JURISDICTION

The opinion and order of the Court of Appeals for the Fifth Circuit were entered on August 8, 1975. Petitioners' Motions for Rehearing and Rehearing En Banc were denied on October 3, 1975. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

QUESTIONS PRESENTED

Important Undecided Questions of Federal Law.

1. In light of the Supreme Court decision in *United Housing Foundation, Inc.* v. *Forman*, ... U.S. ....., 95 S.Ct. 2051 (1975), was the Fifth Circuit mistaken in holding that because the transaction alleged *literally* fell within the definition of "sale" found within the Securities Exchange Act, the District Court could not determine that *in fact* no "sale" of securities had actually taken place?

2. Since jurisdiction over divorce and domestic relations belongs exclusively to the laws of the states, when a federal district court determines that the transaction complained of is part of an indivisible divorce and property settlement, do the federal courts have jurisdiction to hear a complaint alleging a violation of the Securities Exchange Act of 1934?

Conflict of Decisions in the Courts of Appeals.

3. When a District Court decides a Motion to Dismiss for Lack of Subject Matter Jurisdiction must it accept the allegations of the complaint as true, even though such allegations are controverted, or can it ascertain the actual facts and dismiss the case if these facts show that no federal jurisdiction exists despite the formal sufficiency of the pleadings? The Fifth Circuit has held that a District Court must accept the allegations in a Plaintiff's complaint as true, contrary to earlier decisions by the Supreme Court and the Third, Fourth, Sixth and Tenth Circuit Courts of Appeals.

STATUTES AND RULES INVOLVED

This case involves Sections 3(a)(14) and 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78c(a)(14) and 15 U.S.C. § 78j(b), and Rule 10b-5 promulgated by the Securities and Exchange Commission, 17 C.F.R. 240.10b-5. The case also involves Rule 12(b)(1), Federal Rules of Civil Procedure. All of these Statutes and Rules are reprinted herein in Appendix C, *infra,* pp. 23a through 25a.

STATEMENT OF THE CASE

1. Factual Background.

On December 8, 1969, Doris Barshop Spector filed suit for divorce against Bernard D. Spector in 166th District Court of Bexar County, Texas. For the next two years, their attorneys attempted to negotiate a property settlement. The property settlement was extremely complicated because Doris Barshop Spector, her family and her two brothers (who are also Petitioners in this cause of action), each owned interests in numerous properties, partnerships and corporations. The parties to the divorce dis-

agreed over whether Mrs. Spector's interests in these business entities were her separate property or community property. One of the corporations involved was Barshop Motel Enterprises, Inc. (B.M.E.), a corporation engaged in the business of owning and operating motor inns. Mrs. Spector owned in her name one-third of the issued and outstanding shares of B.M.E.

In October, 1971, the parties reached general agreement about the broad outline of a property settlement. On October 20, 1971, a nonbinding outline was prepared of the settlement discussions. This draft outline stated that Mr. Spector would receive as part of an overall settlement of the divorce and property rights of the Parties "$400,000.00 'worth' of cash and/or properties and/or business interests". One problem in the settlement negotiations concerned the source of the $400,000.00 to be paid to Mr. Spector. Further meetings were held in November and December, 1971. Although Mrs. Spector owned numerous valuable properties, she did not personally have that amount of cash. The parties reached agreement at a settlement conference held December 15, 1971. This agreement was summarized in a letter dated December 17th, written by Mr. Spector's attorney, to Mrs. Spector's attorney. The pertinent parts of this letter state:

> "Under the proposed settlement agreement the following assets will be received . . . by Bernard Spector:
>
> 1. $400,000.00 in properties and/or business interests, such properties and/or business interests to be received as the parties shall agree to, and which are to be purchased as set out in paragraph 7 below. . . .
>
> 7. Any purchase of properties and/or business interests awarded to Bernard Spector under the settlement agreement shall be purchased subsequent to the entry of the divorce decree and paid on the following basis . . ."

As the letter of December 17, 1971, clearly shows, Mr. Spector did not know what assets he would receive which he would in turn "sell" for $400,000.00. The parties subsequently agreed that the business interests which Mr. Spector would receive and immediately sell back to the Petitioners would be eighteen shares of stock in B.M.E., which were less than half of the forty shares of B.M.E. that Mrs. Spector owned. Although Mr. Spector eventually received shares of B.M.E., he might equally as well have received any other asset which the Petitioners would then have bought for the identical price, as previously agreed to.

It is also plain from this letter that the $400,000.00 did not represent an agreed value of the eighteen shares of B.M.E., but was rather a sum payable to Mr. Spector in partial settlement of all of his claims against all of his wife's property. The thrust of the settlement agreement was to place $400,000.00 in cash in Mr. Spector's hands. The use of B.M.E. stock was a means of funding the settlement. The parties first agreed on the dollar figure to be received by Mr. Spector and then determined mechanical means (and source of funds) to accomplish this result.

The Property Settlement, Support and Maintenance Agreement was executed and acknowledged by the parties and approved by their counsel on March 16, 1972. The 166th District Court of Bexas County, Texas, entered its divorce judgment, of which the property settlement was a part, at 1:30 p.m. that day.[1] The parties to the divorce then left the courthouse and proceeded to a nearby bank.

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[1] This was a contractual judgment which under Texas law had no decretal value, but merely carried out and approved the contract of the parties. *Edwards* v. *Gifford,* 155 S.W.2d 786 (Tex., 1941); *Wright* v. *Allstate Insurance Company,* 285 S.W.2d 376 (Tex. Civ.App.-Dallas, 1955) writ ref'd, n.r.e.; *Empire Gas & Fuel Co.* v. *Railroad Commission of Texas,* 94 S.W. 2d 1240 (Tex. Civ.App.-Austin, 1936) writ ref'd.

There they signed the fourteen other instruments, all prepared and approved prior to the divorce, which were necessary to effectuate the terms of the divorce decree and property settlement. One of these instruments was the previously contracted to "sale" of eighteen shares of B.M.E. stock from Bernard Spector to the corporation. This agreement was signed by the Parties less than an hour after the divorce and property settlement was entered by the Court. At that point, Mr. Spector was handed a B.M.E. certificate which he then endorsed back to the corporation. The eighteen shares of B.M.E. stock were never in Mr. Spector's possession for more than the few seconds necessary for him to sign the previously prepared endorsement on the stock certificate. He received cash, notes and other consideration as set out in the property settlement agreement and the agreement for the purchase of B.M.E. stock.[2]

Both parties and their counsel agreed upon a dollar amount and only after that dollar amount was decided did they agree that the funds to pay such amount would come from B.M.E. All of the documents to effectuate the overall property settlement agreement, including the stock "purchase" were drafted, approved and agreed to over a three month period prior to the divorce.

---

[2] The property settlement agreement, the divorce judgment and all of the documents executed to carry it out, including the "sale" of the B.M.E. stock, were, under the Texas law, one contract. *Guadalupe-Blanco River Authority* v. *City of San Antonio*, 200 S.W. 2d 989 (Tex., 1947); *Peterson* v. *Miller Rubber Company of N.Y.*, 24 F.2d 59 (8th Cir., 1928); *Veal* v. *Thomason*, 159 S.W.2d 472 (Tex., 1942); *V.H. Pritchard* v. *Nelson*, 147 F.2d 939 (4th Cir., 1945); *Board of Insurance Commissioners* v. *Great Southern Life Ins. Co.*, 239 S.W.2d 803 (Tex., 1951); and *Bowersock Mills & Power Co.* v. *Commissioner of Int. Rev.*, 172 F.2d 904 (10th Cir., 949). Respondent did not challenge these authorities, except by an unsupported assertion that the B.M.E. stock purchase was a separate legal transaction.

After the divorce, in the forty-five minutes which elapsed between its entry and the signing of the agreement to purchase B.M.E. stock, there were no negotiations regarding whether the previously agreed to B.M.E. stock transaction would occur or as to the amount of money involved. Mr. Spector did not have the option of refusing to transfer the stock of B.M.E.

The transfer of the stock was the automatic result of the agreement reached before the divorce judgment was entered, and was an integral part of the indivisible divorce and property settlement. Within an hour after the divorce, the pre-arranged B.M.E. stock transaction was carried out for the pre-arranged dollar amount at the pre-arranged time.

In March, 1973, B.M.E.'s assets were acquired by L Q Motor Inns, Inc., ("L Q"), subject only to stated liabilities, which did not include any liability to the Respondent. Shortly thereafter L Q became a "public company" by means of a sale of its shares in a public offering. L Q did not exist at the time of the divorce and property settlement. It was formed out of the assets of B.M.E. and more than forty other individuals, partnerships and corporations.

2. Proceedings Below.

On November 16, 1973, Bernard Spector filed a complaint in the Western District of Texas against Petitioners alleging several causes of action. Jurisdiction of the District Court was invoked under the Securities Exchange Act of 1934 (15 U.S.C. § 78aa). The first cause of action alleged a violation of Section 10(b) of the 1934 Act, and Rule 10b-5. The second through fifth causes of action alleged various state claims and sought to invoke the District Court's pendent jurisdiction.

On January 15, 1974, the Petitioners filed a Motion to Dismiss for Lack of Subject Matter Jurisdiction, to which they attached numerous exhibits and affidavits, together with their supporting brief. Subsequent to that date, the Respondent filed an amended complaint, a brief on the legal issues involved and affidavits and exhibits of his own. A hearing was held on Petitioners' Motion to Dismiss on April 24, 1974, at which time the Court heard extensive oral arguments from counsel. On May 7, 1974, the Court entered a Memorandum Opinion dismissing the Respondent's claim for lack of subject matter jurisdiction. On the basis of the exhibits and the affidavits before it, the Court disregarded the allegations in the Respondent's complaint and found that the alleged stock purchase agreement was an indivisible part of a divorce and property settlement. The Court further found that the transaction complained of was not a "sale" within the meaning of the Federal Securities Law.

The Respondent appealed the trial court's decision to the Fifth Circuit. On August 8, 1975, the Fifth Circuit reversed the opinion of the District Court and remanded the case for further proceedings. The Fifth Circuit denied Petitioners' Motions or Rehearing and Rehearing En Banc on October 3, 1975. The Fifth Circuit took the position that the well-pleaded *allegations* in the Respondent's complaint must be accepted as true. This necessarily cut off any inquiry into whether the jurisdictional *facts* in actuality supported the jurisdictional *allegations* of a federal cause of action.

REASONS FOR GRANTING THE WRIT

I.

IN LIGHT OF THE SUPREME COURT'S DECISION IN *UNITED HOUSING FOUNDATION, INC.* v. *FORMAN*, THE FIFTH CIRCUIT WAS MISTAKEN IN RULING THAT BECAUSE PART OF THE TRANSACION COMPLAINED OF IN THIS CASE FELL WITHIN THE LITERAL DEFINITION OF A "SALE", THE DISTRICT COURT COULD NOT DETERMINE THAT IN FACT NO SALE OF SECURITIES HAD ACTUALLY TAKEN PLACE.

The District Court held that no "sale" of stock within the meaning of the Federal Securities laws had taken place. The District Court reached this conclusion after studying all of the evidence, affidavits and exhibits presented to it. The uncontradicted evidence before it revealed that in partial settlement of all of his claims against all of his wife's property in numerous properties, partnerships and corporations, the Respondent agreed to receive $400,000.00 in cash, in an unspecified property, or in business interests. It later became apparent that Mrs. Spector could not raise $400,000.00 in cash and the Respondent agreed to accept property or business interests which he would then *immediately* sell after the divorce for the agreed amount. Thus, in December, 1971, the Respondent agreed to receive an unknown asset which he would then sell for a prearranged price. The District Court rightly concluded that no fraud in connection with a "sale" of stock has occurred when an individual agrees to sell an unknown asset to be chosen later for a prearranged price.

It is implicit in the concept of a "sale" under the Federal Securities Laws that at the time the price is agreed on, the "seller" know he is selling securities. Conversely stated, the

principle should be that there is no sale of a "security" where there is an agreed overall settlement calling for delivery of a then-unspecified asset to a then-unspecified buyer for a specified amount, and *later* the asset chosen to accomplish such "settlement" is corporate stock. Respondent was not an investor in securities nor was he engaged in a securities transaction. He was merely engaged in settling his divorce and he now attempts to use the Federal courts to secure more than his settlement provided from his wife, her brothers, and the lawyer who represented them.

The decisions of this court have made it clear that the principal purpose of the Federal Securities laws is to protect the interests of the investor in securities. This point was made in *Superintendent of Insurance of the State of New York* v. *Banker's Life & Casualty Co.*, 404 U.S. 6 (1971), when the Supreme Court maintained at 13:

> "The crux of the present case is that Manhattan suffered an injury as a result of deceptive practice touching its sale of securities as an investor."

See *Kahan* v. *Rosenstiel*, 424 F.2d 161, 173 (3rd Cir., 1970). It is the economic reality of the transaction that is important, and not the labels that are affixed to it. As the Supreme Court pointed out in *Tcherepnin* v. *Knight*, 389 U.S. 332 (1967) at 336:

> "[I]n searching for the meaning and scope of the word 'security' in the Act[s], form should be disregarded for substance and the emphasis should be on economic reality."

The District Court used this standard in ascertaining the significance of the transactions of which the Respondent complained. It found that the stock purchase agreement was an integral part of an indivisible divorce settlement. It knew that the Respondent had agreed to sell an

unknown asset for a prearranged price before he knew that asset would be B.M.E. stock. Dealing with the substance of the transaction and disregarding its form, the court concluded that no "sale" had taken place within the meaning of the Federal Securities laws. It is apparent that this decision reflects the economic reality of the transaction. How could anything the Petitioners might have said or omitted to say in relation to B.M.E. constitute a fraud on Respondent that induced him to sell B.M.E. stock at a lower price than he otherwise would have, when the price was agreed upon before the Respondent even knew that it was B.M.E. stock he was talking about?

In its opinion, the Fifth Circuit did not engage in any analysis of the economic reality of the transactions. It made no attempt to separate the form of the stock purchase agreement from its substance. It did not dispute the District Court's finding that the suit arose out of a divorce property settlement. In fact, it agreed that this was the case. Instead, it employed a purely mechanical test to determine whether the transaction complained of fell within the definition of "sale" found within the Securities Exchange Act (15 U.S.C. § 3(a)(14)). The court then concluded, at 285:

> "To label this transaction a 'sale' requires no strained construction of that term."

Assuming, *arguendo,* that the transaction which is the basis of this law suit falls within a literal definition of the term "sale", that is not the end of the inquiry as the Fifth Circuit assumed. The question remains whether the transaction is the type intended to be covered by the Securities Exchange Act. The statute is not to be applied mechanically, without concern for its intent and purpose.

This was made clear by the Supreme Court just this year in its landmark decision in *United Housing Foundation, Inc.* v. *Forman,* ..... U.S. ....., 95 S.Ct. 2051 (1975). This case was decided after the instant cause of action had already been briefed and argued before the Fifth Circuit. In *Forman,* the plaintiffs were tenants in cooperative apartments. In order to buy an interest in the project which entitled them to apartments in the cooperative, they had to purchase shares of stock in the corporation building the project. The plaintiffs later sued under Rule 10b-5 and claimed that the rents charged them were higher than promised by the corporation at the time it sold them its stock. The defendants moved to dismiss for lack of subject matter jurisdiction, claiming that the shares of stock involved were not "securities" within the meaning of the Securities Exchange Act. They argued that the sole purpose of the individuals purchasing stock was to acquire an apartment rather than to make an investment. They noted that it was virtually impossible to make a profit on the stock because every tenant at the time he moved out of the apartment cooperative had to offer his stock back to the corporation at the price he had purchased it. The Supreme Court analyzed the situation in some depth, looked at the substance of the situation rather than its form, placed its emphasis on the economic realities and concluded that the stock which was the subject of the suit was not a "security" within the meaning of the Securities Exchange Act. It reached that decision despite the fact that the transaction involved dealt with shares of something called "stock", just as in the instant case the transaction involved was called a "purchase and sale". The Supreme Court explained its reasons for this decision at 2058-2059:

> "We reject at the outset any suggestion that the present transaction, evidenced by the sale of shares called

> 'stock' must be considered a securities transaction simply because the statutory definition of a security includes the words 'any . . . stock'. Rather we adhere to the basic principle that has guided all of the Court's decisions in this area: '[I]n searching for the meaning and scope of the word "security" in the Act[s], form should be disregarded for substance and the emphasis should be on economic reality.' Tcherepnin v. Knight, 389 U.S. 332, 336, 88 S.Ct. 548, 19 L.Ed. 2d 564 (1967). . . .
>
> The primary purpose of the Securities Acts of 1933 and 1934 was to eliminate serious abuses in a largely unregulated securities market. The focus of the Acts is on the capital market of the enterprise system: the sale of securities to raise capital for profit-making purposes, the exchanges on which securities are traded, and the need for regulations to prevent fraud and to protect the interest of investors. Because securities transactions are economic in character Congress intended the application of these statutes to turn on the economic realities underlying a transaction, and not on the name appended thereto. Thus, in construing these Acts against the background of their purpose, we are guided by the traditional canon of statutory construction: 'that a thing may be within the letter of the statute and yet not within the statute, because not within its spirit, nor within the intention of its makers.' Church of the Holy Trinity v. United States, 143 U.S. 457, 459, 12 S.Ct. 511, 512, 36 L.Ed. 226 (1892). See also United States v. American Trucking Assns., Inc., 310 U.S. 534, 543, 60 S.Ct. 1059, 1063, 84 L.Ed. 1345 (1940)."

Based on this standard, Petitioners contend that the divorce property settlement which is the basis of this suit can clearly be seen to fall outside the scope of the Federal Securities laws, even though one part of the entire divorce property settlement has been labeled a "purchase and sale" of stock.

The *Forman* case dealt with the meaning of the word "security" within the context of Rule 10b-5. However, other decisions in recent years express the same philosophy that it is the economic reality of the transaction that governs rather than the name by which it is called. In *Kern County Land Co.* v. *Occidental Petroleum Corp.*, 411 U.S. 582 (1973), the Supreme Court dealt with the issue of whether, in the context of Section 16(b) of the Securities Exchange Act, the word "sale" must be given a literal interpretation. Once again, the court examined the economic realities, dealing with the substance of the transaction involved, rather than its form. The court concluded at 594-595:

> "In deciding whether borderline transactions are within the reach of the statute, the courts have come to inquire whether the transaction may serve as a vehicle for the evil which Congress sought to prevent — the realization of short-swing profits based upon access to inside information — thereby endeavoring to implement congressional objectives without extending the reach of the statute beyond its intended limits. . . . Thus, '[i]n interpreting the terms 'purchase' and 'sale,' courts have properly asked whether the particular type of transaction involved is one that gives rise to speculative abuse.' Reliance Electric Co. v. Emerson Electric Co., *supra,* 404 U.S., at 424 n. 4, 92 S.Ct., at 600."

Applying this standard of analysis, the court held the transaction complained of did not fall within the scope of Section 16(b), even though a "sale" literally occurred. Thus, while interpreting another section of the same law, the Supreme Court decided that the exact term which is involved here ("sale") should not be applied literally.

The Second Circuit has already considered the question of whether the term "sale" should be given a literal interpretation in the context of Section 10(b) and Rule 10b-5.

In *International Controls Corp.* v. *Vesco,* 490 F.2d 1334 (2nd Cir., 1974), cert. denied, 417 U.S. 932 (1974), the Second Circuit held that in deciding whether a transaction fell within the subject matter jurisdiction of the Federal courts under Section 10(b) and Rule 10b-5, the term "sale" could not be literally interpreted. The court observed at 1346:

> "We therefore reject our dissenting brother's paean to literalness in construing the term 'sale' to require the passage of consideration in order to inject the requisite significance into the disposition of securities. Learned Hand wisely counseled: 'Of course it is true that the words used, even in their literal sense, are the primary, and ordinarily the most reliable, source of interpreting the meaning of any writing: be it a statute, a contract, or anything else. But it is one of the surest indexes of a mature and developed jurisprudence not to make a fortress out of the dictionary; but to remember that statutes always have some purpose or object to accomplish, whose sympathetic and imaginative discovery is the surest guide to their meaning.' Cabell v. Markham, 148 F.2d 737, 739 (2d Cir. 1945)."

This, of course, is the very issue which must be determined in the instant cause of action.

Also applicable to this case is the decision of the Supreme Court in *Blue Chip Stamps* v. *Manor Drug Stores,* ..... U.S. ....., 95 S.Ct. 1917 (1975), which considered who could qualify as a plaintiff under a private cause of action for damages for violation of Rule 10b-5. In *Blue Chip,* the court held that it is only persons who are purchasers and sellers of *securities* who can properly be plaintiffs and stated, at 1925:

> ". . . [J]ustification is absent when there is no actual purchase or sale of securities, or a contract to do so, affected or tainted by violation of § 10(b)."

Since *Blue Chip* does require that one be an actual purchaser or seller of *securities*, it would appear that to be such a "seller", one must know at the time the price is agreed on that he is selling a *security*, rather than an unknown asset to be agreed on later. Here, Respondent made no such showing and could not do so.

In *Forman*, the Supreme Court held that the term "security" could not be given a literal and mechanical application in the context of Section 10(b) and Rule 10b-5. In *Kern County Land Co.*, the Supreme Court held the term "sale" could not be given a literal and mechanical application in the context of Section 16(b). In *International Controls Corp.*, the Second Circuit held that the term "sale" could not be given a literal and mechanical application in the context of Section 10(b) and Rule 10b–5. It is time that the Supreme Court extended the doctrine that substance rules over form and the economic realities of the situation must be looked at to cover the definition of the word "sale" within the context of Section 10(b) and Rule 10b-5.

The position adopted by the Fifth Circuit runs counter to this entire trend in Federal Securities law. The language which the Fifth Circuit used in its decision makes it clear that the court, unlike the trial court below, made no attempt to analyze the economic realities of the transaction to decide what its substance was, and this is the test which the Supreme Court approved and applied, in the *Forman* and *Kern County Land Co.* cases. Nevertheless, the Fifth Circuit based its decision upon the fact that the stock transaction fell within the literal definition of a "sale".

Prior to the Supreme Court's decision in *Forman*, there was some precedent for taking the "literal" approach. Indeed, a different panel of the Second Circuit than the one which decided the *International Controls Corp.* case used

this exact standard when it heard the *Forman* case below. In *Forman* v. *Community Services, Inc.*, 500 F.2d 1246 (2nd Cir., 1974), the Second Circuit held at 1252:

> "One basis for such a finding is the so-called literal approach. . . . According to this approach the fact that 'stock' certificates are used in a 'stock' corporation is sufficient in itself to bring transactions in the 'stock' within the literal definition of the Acts. . . . 'When a stock corporation is used the securities acts literally apply, even though the profit motive is not dominant.' Professor Loss has put it, 'When the ownership of an individual apartment is evidenced by stock in the co-operative, as it usually is, the federal and state securities statute would seem literally to apply' 1 L.Loss, Securities Regulation 492-93 (2d ed. 1961) (footnotes omitted). Judge Mansfield as a district judge supported the literal application of specific definitions of securities so as to *include* instruments within the coverage of the acts. Movie-lab, Inc. v. Berkey Photo, Inc., 321 F.Supp. 806 (S.D.N.Y. 1970) aff'd, 452 F.2d 662 (2d Cir. 1971). The Supreme Court said in SEC v. C. M. Joiner Leasing Corp., 320 U.S. 344, 351 64 S.Ct 120, 123, 88 L.Ed. 88 (1943), reaffirmed in Tcherepnin v. Knight, 389 U.S. at 339, 88 S.Ct. 548, 'In the Securities Act the term "security" was defined to include by name or description many documents in which there is common trading for speculation or investment. Some, such as notes, bonds and stocks, are pretty much standardized and the name alone carries well-settled meaning. . . . *Instruments may be included within any of these definitions as a matter of law, if on their face they answer to the name or description.* However, the reach of the Act does not stop with the obvious and commonplace. . . .' (emphasis added [by the Second Circuit]). This language gives support to the proposition that if a given instrument is a share of stock 'on its face' it is literally within the ambit of the statute."

The Second Circuit applied this standard and was told by the Supreme Court that it had erred in so doing. It

should not have adopted a literal definition of the term "stock", but instead should have examined the economic realities of the situation before it.

Since *Forman* was decided after this case was heard, the Fifth Circuit, applying the same standard as the Second Circuit in *Forman*, was in error when it decided that the transaction complained of here was a "sale" of securities merely because literally the transaction would seem to fall within the scope of the Securities Exchange Act. Thus, the Fifth Circuit did exactly what the Supreme Court held was error in *Forman*.

II.

THE FIFTH CIRCUIT HAS SUMMARILY EXTENDED THE SECURITIES EXCHANGE ACT TO COVER TRANSACTIONS WHICH ARE AN INTEGRAL PART OF AN INDIVISIBLE DIVORCE AND PROPERTY SETTLEMENT, CONTRARY TO THE LONGSTANDING FEDERAL POLICY LEAVING THE ENTIRE FIELD OF DIVORCE AND DOMESTIC RELATIONS TO THE STATE COURTS.

The Fifth Circuit dismissed the contention that the purchase of stock agreement which is the basis of the Respondent's suit was part of an indivisible divorce and property settlement in two sentences. It held, at 282:

> "To be sure, this case presents a novel factual setting for a federal claim for securities fraud, as it arises out of a property settlement in a divorce action. Although the divorce and its attendant property settlement are conrolled by state law, plaintiff's 10b-5 claim falls

> within the subject matter jurisdiction of the federal courts."

In reaching this position, the Fifth Circuit rejected the century old doctrine that the entire field of divorce and domestic relations is within the exclusive jurisdiction of the state courts.

It is a long established principle of federal law that the federal courts do not have jurisdiction in divorce cases. This rule was stated by the Tenth Circuit in *McCarty* v. *Hollis*, 120 F.2d 540 (10th Cir., 1941) at 542:

> "A United States court is without jurisdiction to grant divorces or annul marriages. It has been consistently said without deviation that the field of domestic relations affecting husband and wife, or parent and child, belongs exclusively to the laws of the states."

In *Lutsky* v. *Lutsky*, 310 F.Supp. 517 (S.D. Fla., 1970), the plaintiff attempted to evade this doctrine by claiming that she was not seeking a divorce, but rather a "declaration" of her marital status. The court dismissed for lack of jurisdiction, holding at 519:

> "The [diversity] statute, however, has had carved from it two judicially made exceptions—divorce and probate —where the federal court will not act even though diversity is present. . . .
>
> We disclaim altogether any jurisdiction in the courts of the United States upon the subject of divorce."

In *Gargallo* v. *Gargallo*, 472 F.2d 1219 (6th Cir., 1973), the plaintiff sought to litigate child custody, rather than a divorce decree itself. Nevertheless, the court rejected his claim that it had jurisdiction to hear his case. It maintained at 1220:

> ". . . [T]his court is bound by the long standing exception to the statute that Federal Courts will not accept jurisdiction in domestic relations cases. . . . 'The whole subject of the domestic relations of husband and wife, parent and child, belongs to the laws of the states, and not to the laws of the United States.'" [citing in re Burris, 136 U.S. 586]

The court in *Shiffman* v. *Askew,* 359 F.Supp. 1225 (M.D.Fla., 1973) aff'd *sub nom Makres* v. *Askew,* 500 F.2d 577 (5th Cir., 1974), concluded at 1229, 1231:

> "From the inception of our federal system . . . the Supreme Court has consistently recognized the unique status of marriage and divorce as involving a myriad of socio-legal ramifications, virtually all of which are left to the exclusive province of the states. In 1858, the court declared: '. . . we disclaim altogether any jurisdiction in the courts of the United States upon the subject of divorce, or for the allowance of alimony . . .' Barber v. Barber, 62 U.S. (21 How.) 582, 584, 16 L.Ed. 226 (1858). . . .
>
> The significance of these authorities vis-a-vis the present case is threefold. First, it is indelibly ingrained in our federal system that the entire field of marriage and divorce is left to the individual regulation of the several states."

This century old doctrine has recently been affirmed by the Supreme Court in *Sosna* v. *Iowa,* 419 U.S. 379 (1975). In *Sosna,* Iowa's divorce residency requirement came under attack. In upholding the Iowa law, the court observed at 386:

> "The durational residency requirement under attack in this case was a part of Iowa's comprehensive statutory regulation of domestic relations, an area that has long been regarded as a virtually exclusive province of the States. Cases decided by this court over a period of more than a century bear witness to this historical fact."

The Plaintiff in *Sosna* contended that Iowa's durational requirement was unconstitutional. No such claim can be made in the instant cause of action, since the Federal Securities laws are of statutory rather than constitutional origin. Thus, once again the Supreme Court has reaffirmed the doctrine that the entire field of domestic relations is within the sole jurisdiction of the state courts, as long as the Constitution is not violated.

The Fifth Circuit recognized that the Respondent's cause of action arose out of a divorce property settlement (at page 282). However, it off-handedly dismissed the significance of this fact with the bald assertion that nevertheless the Respondent's claim fell within the subject matter jurisdiction of the federal courts. Under the doctrine cited above, however, if the transaction is truly an integral part of an indivisible divorce and property settlement, then the federal courts can have no jurisdiction over it, no matter what labels the Respondent decides to use. In *Lutsky,* the plaintiff called her complaint a suit for a "declaration" of her martial status, rather than a suit for a divorce. In the instant case, the Respondent has chosen to label his claim a suit for securities fraud, rather than a suit to reopen and improve his entire divorce property settlement. Nevertheless, if in fact it is a suit to reopen his divorce property settlement, then the label which Respondent attaches is entirely irrelevant.

The district court, after considering the affidavits and exhibits, concluded that the transaction complained of was an integral part of an indivisible property settlement. Nothing in the Fifth Circuit's opinion in any way intimates that the district court was in error in reaching this conclusion based on the evidence before it. Without considering the point or citing a single authority, dealing with a case which

it admitted (at page 282) presented a novel factual setting for a federal claim of securities fraud, the Fifth Circuit overturned a doctrine which has endured for more than a century and has been reaffirmed by the Supreme Court only this year.

The implications of this hastily arrived at holding are serious in the extreme. The holding will drastically change the laws relating to divorce settlements, particularly in Texas and other community property states. At any time afer a divorce property settlement where corporate stock is involved, a party who later becomes dissatisfied will be able to claim the benefits of some portions of the property settlement and attempt to use the Federal courts to improve that part of the settlement which involves corporate stock without reopening the entire settlement. Under Texas law, when a property settlement is reopened all portions of the settlement come before the court, not merely those with which the plaintiff is dissatisfied. *Smith* v. *Smith*, 468 S.W.2d 139 (Tex. Civ. App.-Dallas, 1971) no writ history. Under the Fifth Circuit's holding, the parties to every such divorce, their families and their counsel will be subject to new broad, undefined responsibilities and liabilities imposed upon them because they participate in the divorce process—a matter which all the parties in this case concede is governed by state law—simply because the property settlement partially involves corporate stock.

Either party to a divorce suit in which corporate stock is involved will be able to work out the best settlement which said party can obtain and then have access to the federal courts to improve his settlement, free of the burden (and of the risk) imposed upon him in the state courts, which would reopen the entire settlement and not just a portion of it. The federal courts will thus become courts of second resort for former divorce litigants to improve

part of their settement without reopening the entire property agreement, and without the accompanying risk that such complainant might be treated less favorably in that event.

It has always been a judicial policy of the federal courts to promote finality of judicial decisions. To allow plaintiffs to relitigate their property settlements in federal court would be to open a Pandora's box by vastly expanding the scope of the Federal Securities laws. No divorce property settlement will ever become final until the appropriate statute of limitations applicable to Rule 10b-5 suits has expired. The creation of such turmoil will serve no useful end and will undermine the previous exclusive jurisdiction of state courts in divorce cases. Such a result is particularly unnecessary since the Respondent in this case has a perfectly adequate remedy in the courts of the State of Texas, where, if he wishes, he can assert the alleged fraud and relitigate his divorce property settlement to his heart's content.

The decision of the Fifth Circuit presents a new and important question of federal law for the Supreme Court to decide. As the Fifth Circuit acknowledged, the Respondent's alleged cause of action presents a novel factual setting for a claim of securities fraud. As far as the Petitioners are aware, it is the first case in which the alleged securities fraud was an integral part of an indivisible divorce property settlement. It would thus be appropriate for the Supreme Court to decide whether such a transaction is covered by the Federal Securities laws. Moreover, this is a question of wide general import. Numerous divorce property settlements involving corporate stock are agreed to every year in Texas and in other states. The precedent which the Fifth Circuit has so off-handedly created would apply to each and every one of these property settlements, too.

III.

THE FIFTH CIRCUIT'S REFUSAL TO LOOK BEHIND THE ALLEGATIONS IN THE RESPONDENT'S COMPLAINT CONFLICTS WITH PREVIOUS DECISIONS OF THE SUPREME COURT AND THE THIRD, FOURTH, SIXTH AND TENTH CIRCUIT COURTS OF APPEALS AS TO THE PROPER PROCEDURE TO BE EMPLOYED WHEN A MOTION TO DISMISS FOR LACK OF SUBJECT MATTER JURISDICTION CHALLENGES THE JURISDICTIONAL FACTS ALLEGED.

The central pivot upon which the Fifth Circuit's decision turns is its holding that on an appeal from dismissal for lack of jurisdiction, the allegations of the complaint must be taken as true. The trial court did not follow this course of action. It received evidence in the form of affidavits and exhibits and it determined issues of fact. It decided that contrary to the allegations in the complaint the so-called "sale" of stock was part of an indivisible divorce and property settlement, and that the transaction in question was not a "sale" within the meaning of the Federal Securities Laws. The Fifth Circuit did not conclude that the trial court had wrongly decided these issues of fact. but held that the trial court *could not even consider them.* It held that the well-pleaded allegations in the complaint *had* to be accepted as true. Therefore, the evidence which the Petitioners introduced to prove the contrary was not considered by the Fifth Circuit.

The position taken by the Fifth Circuit flatly contradicts earlier rulings of the Supreme Court and four other Courts of Appeal. The Supreme Court made it absolutely clear that Plaintiff's allegations do not control on a motion to dismiss for lack of subject matter jurisdiction in *McNutt* v. *General Motors Acceptance Corporation,* 298 U.S. 178 (1936). The court held at 184:

> ". . . [T]he trial court is not bound by the pleadings of the parties, but may, of its own motion, if led to believe that its jurisdiction is not properly invoked 'inquire into the facts as they really exist.' "

The Supreme Court further amplified Plaintiff's responsibility in connection with alleging jurisdictional facts at 189-190:

> "He must allege in his pleading the facts essential to show jurisdiction. If he fails to make the necessary allegations he has no standing. If he does make them, an inquiry into the existence of jurisdiction is obviously for the purpose of determining whether the facts support his allegations. In the nature of things, the authorized inquiry is primarily directed to the one who claims that the power of the Court should be exerted in his behalf. As he is seeking relief subject to this supervision, it follows that he must carry throughout the litigation the burden of showing that he is properly in court. *The authority which the statute vests in the court to enforce the limitations of its jurisdiction precludes the idea that jurisdiction may be maintained by mere averment or that the party asserting jurisdiction may be relieved of its burden by any formal procedure.* If his allegations of jurisdictional facts are challenged by his adversary in any appropriate manner, he must support them by competent proof." (emphasis supplied)

Three years later, in *Gibbs* v. *Buck,* 307 U.S. 66 (1939), the Supreme Court reiterated that the trial court can go behind the allegations to determine the facts. The court maintained at 72:

> ". . . [T]he burden of showing by the admitted facts that the Federal Court has jurisdiction rest upon the complainants. If there were any doubt of the good faith of the allegations, the court might have called for their justification by evidence. . . ."

The same position has been adopted by several Courts of Appeals which have considered the issue. The Third Circuit stated the basic rule in *Shahmoon Industries, Inc.* v. *Imperato,* 338 F.2d 449 (3rd Cir., 1964) at 451:

> "'. . . On every writ of error or appeal the first and fundamental question is that of jurisdiction, first, of this court, and then of the court from which the record comes. . . .' The rule applies even though the pleadings are sufficient but the record does not support the allegations."

If the record does not support the jurisdictional allegations, the case should be dismissed for lack of jurisdiction.

The Third Circuit considered the problem again in *Local 336, American Fed. of Musicians, AFL-CIO* v. *Bonatz,* 475 F.2d 433 (3rd Cir., 1973). There, the court reversed the finding of lack of subject matter jurisdiction. It did not do so, however, because the allegations of the complaint must be taken as true. Instead, it reversed because the trial court had not given the Plaintiff an opportunity to present his version of the facts before the case was dismissed. The central issue in the case was whether the contract involved fell within the coverage of Section 301 of the Labor-Management Relations Act of 1947. The trial court held the contract did not fall within the Act and dismissed the case for lack of jurisdiction. The Third Circuit reversed, maintaining at 437-438:

> "The jurisdictional issue having been raised at this juncture we can not say that as a matter of law Exhibit A is a § 301 contract. We hold only that it was error for the district court to decide that issue with this record on a *sua sponte* Rule 12(b)(1) motion. We recognize that the district courts have more latitude as to modes of proof and the disposition of issues of jurisdictional fact. . .. But we have never departed from the

> rule that even on such an issue the record must clearly establish that after jurisdiction was challenged the plaintiff had an opportunity to present the facts by affidavit or by deposition, or in an evidentiary hearing, in support of his jurisdictional contention. . . .The existence of an agreement between a labor organization and an employer is, for § 301 purposes, a jurisdictional fact. For the determination of that fact, no doubt, those more liberal modes of proof apply which the Supreme Court has approved for jurisdictional determination. Whether the court proceeds by considering affidavits or depositions or by an evidentiary hearing, however, something must appear of record to contradict the pleaded and uncontroverted jurisdictional allegation that there was a § 301 contract and support the District Court's determination."

The case was reversed because the plaintiff had not been given a chance to present evidence to convince the district court that the conract fell within §301 of the Labor-Management Relations Act. However, the Third Circuit's decision makes it plain that if after considering all the evidence, the trial court then concluded that there was no contract within the scope of §301, the case should be dismissed for lack of subject matter jurisdiction even though the jurisdictional allegations in the plaintiff's complaint were sufficient.

The Fourth Circuit reached the same conclusion in *Prack* v. *Weissinger,* 276 F.2d 446 (4th Cir., 1960) when it observed at 450:

> "The general rule as to the power of the Court to determine its own jurisdiction is stated in 21 C.J.S. Courts § 113 (1940) as follows: 'Every Court has judicial power to hear and determine, or inquire into the question of its own jurisdiction, both as to parties and as to subject matter, and to decide all questions, whether of law or fact, the decision of which is necessary to determine the question of jurisdiction. ***' "

In the instant case, however, the Fifth Circuit has taken the opposite position, thus in effect stripping the district courts of their power to inquire into the fundamental question of their own jurisdiction at a preliminary hearing. The Fifth Circuit is now holding that even if a defendant presents uncontroverted evidence proving that the jurisdictional allegations in the complaint are untrue, the court must nevertheless try the case on the merits.

The case which most closely resembles the instant cause of action is *Spears* v. *Spears,* 162 F.2d 345 (6th Cir., 1947) cert. denied, 332 U.S. 768 (1947). In *Spears,* the appellants filed a complaint which upon its face adequately alleged subject matter jurisdiction. The complaint was carefully drawn to avoid mentioning its true import, which was to invalidate a will which had been accepted for probate by a state court. Probate, like divorce, is an area exclusively within the jurisdiction of the state courts. The appellants in *Spears* made the identical contention which Respondent made to the Fifth Circuit below. The court noted at 347:

> "Appellants contend that the trial court erred in considering the affidavits attached to the Motion to Dismiss, urging that the allegations of the complaint must be taken as true for the purpose of such motion."

Citing *McNutt* v. *General Motors Acceptance Corporation,* the Sixth Circuit flatly rejected this contention. The court went on to explain at 348:

> "But appellants failed to deny and in fact admitted in open court the facts as to the state court's proceedings shown in the affidavits attached to the motions, including the crucial fact that the will of August 27, 1945, a will executed subsequently to that relied on by complainant had been probated. The District Court did not err in considering the affidavits.

> Appellant's complaint is drawn to conceal the fact that they asked this court to set aside the probate of the will of August 27, 1947. The complaint constitutes a colorable attempt to meet Federal jurisdictional requirements in order to oust the state courts of jurisdiction. . . . The jurisdiction to determine the validity of the will lies exclusively in the Michigan courts . . . What appellants ask for is a secondary probate; but this is merely a continuation of a probate proceeding and the Federal Court clearly has no jurisdiction."

Similarly, in the instant case, Respondent's complaint is drawn to allege a federal securities claim. The reality, as revealed in the affidavits and exhibits considered by the trial court, is that the Respondent is seeking to improve his divorce property settlement without reopening the entire settlement, which a Texas Court would have to do. Since divorce is within the exclusive jurisdiction of the state courts, Respondent's remedy lies in the Texas courts, the only courts with jurisdiction to hear it.

The Tenth Circuit also reached the conclusion that the court could go behind the allegations in the complaint to determine if jurisdiction actually exists. In *Praire Band of Pottawatomie Tribe of Indians* v. *Puckkee,* 321 F.2d 767 (10th Cir., 1963), the complaint was drawn to seek recovery under a Federal Statute, but the court found that there was no subject matter jurisdiction. It declared at 770:

> "A genuine and substantial Federal Question must be stated, and the Court will look beyond the naked allegations of the complaint, to determine whether the asserted claim is controlled or conditioned by Federal law."

It is worth noting that the *Shahmoon Industries, Prack,* and *Spears* cases are cases brought into court under diversity jurisdiction, while the *Bonatz* and *Pottawatomie In-*

dians cases were brought into court under Federal question jurisdiction. In both types of cases, the Federal Courts look behind the plaintiff's jurisdictional allegations to determine the true jurisdictional facts.

The above cases can be reconciled with the opinions cited by the Fifth Circuit in its opinion, at 281-282: *Bell* v. *Hood,* 327 U.S. 678, 682-83 (1946); *Dann* v. *Studebaker-Packard Corp.,* 288 F.2d 201, 206 (6th Cir., 1961); *Herpich* v. *Wallace,* 430 F.2d 792, 802 (5th Cir., 1970); and *Mindes* v. *Seaman,* 453 F.2d 197 (5th Cir., 1971). The Fifth Circuit failed to differentiate between the two separate and distinct types of Rule 12(b)(1) motions. The distinction between the two types of Rule 12(b)(1) motions is explained in 5 Wright & Miller, Federal Practice and Procedure: Civil, § 1350 at Page 549:

> "A motion under Rule 12(b)(1) may be used to attack two different types of defects. The first is the pleader's failure to comply with Rule 8(a)(1), which means that te allegations in the complaint are insufficient to show that the Federal Court has jurisdiction over the subject matter of the case. If the complaint does not properly invoke the Court's jurisdiction, then the complaint is defective and unless the deficiency is cured, the motion must be granted regardless of the actual existence of subject matter jurisdiction. *The other defect that may be challenged under Rule 12(b)(1) is the Court's actual lack of jurisdiction over the subject matter, a defect that may exist despite the formal sufficiency of the allegations in the complaint.*" (emphasis supplied)

The same conclusion was reached by the Sixth Circuit in *Spears* v. *Spears, supra,* at 347-348:

> "When a motion to dismiss is used as the equivalent of a demurrer to test the legal sufficiency of the pleadings, no question of fact is presented, and under such circumstances the motion admits the well-pleaded facts of the complaint. . . . But where the motion, as here, traverses the allegations as to jurisdiction and recites

> facts de hors the record, the motion does not constitute an admission of the facts alleged in the complaint. . . . The facts set out in the affidavit attached to the motion to dismiss herein, if true, show that no jurisdiction exists in the Federal court."

In the instant case, the Motion to Dismiss for Lack of Subject Matter Jurisdiction which the petitioners filed is clearly of the second type. Petitioners concede, *arguendo,* that the Respondent's complaint formally alleges a violation of Section 10(b) of the Securities Exchange Act. However, the Petitioners have asserted that these allegations are in fact false and that when the truth was brought before the court in the form of affidavits and exhibits it could be seen that no federal jurisdiction in fact existed.

None of the cases which the Fifth Circuit cited in its opinion are Rule 12(b)(1) motions of the second type. In *Bell* v. *Hood, supra,* the plaintiffs complained of unlawful searches and seizures in violation of the Fourth and Fifth Amendments. The defendants filed a motion to dismiss for failure to state a cause of action and for summary judgment. The district judge, instead, dismissed the suit for want of federal jurisdiction because the action did not arise under the constitution or laws of the United States. The Supreme Court reversed this decision and held, at 681, that since the complaint alleged violations of the Fourth and Fifth Amendments, it was drawn to claim a right to recover under the constitution. *Bell* v. *Hood* simply is not relevant to the problem in the instant case because the defendants did not challenge the truth of the jurisdictional allegations in the plaintiff's complaint and ask the court to determine the actual jurisdictional facts.

In *Dann* v. *Studebaker-Packard Corp., supra,* the defendants filed a motion to dismiss for lack of subject matter

jurisdiction and because the complaint failed to state a claim, and because the complaint failed to comply with the requirements for a class action. It is difficult to ascertain the basis for the decision because, as the court noted at 205:

> "The District Judge granted the motion to dismiss without so much as a hint as to his reason for doing so. As a result, we are now considerably handicapped by not knowing which of the above grounds he relied upon."

However, it is clear that the defendants had not attacked the truth of the complaint's jurisdictional allegations and asked the district court to determine the actual jurisdictional facts. The Court of Appeals made his apparent when it observed at 206:

> "In the case before us, the issues for our consideration all come up on a motion attacking the form of the pleadings. Therefore, the only material necessary for the proper disposition of such a motion is the pleadings themselves, which, of course, are a part of this record."

The Petitioners in this cause of action have not attacked the form of Respondent's pleadings, but instead challenged the truth of the jurisdictional allegations.

In *Herpich* v. *Wallace, supra,* there is no suggestion in the opinion that the defendants challenged the veracity of the jurisdictional allegations of the plaintiff's amended complaint. In the absence of such a challenge, the general rule that the well-pleaded allegations in a plaintiff's complaint must be accepted as true no doubt applies. However, this offers little guidance in deciding a case where the plaintiff's allegations are controverted by a defendant. Moreover, the page cited from *Herpich* by the Fifth Circuit in the instant case makes clear that the principal concern of the

court there was a motion to dismiss for failure to state a claim. The court declared at 802:

> "Moreover, '[i]n appraising the sufficiency of the complaint we follow, of course, the accepted rule that a complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of its claim which would entitle him to relief.'"

In *Mindes* v. *Seaman, supra,* before an answer or any responsive pleading was filed, the court dismissed for want of jurisdiction. Accordingly, at page 198, the Fifth Circuit ruled that the allegations of the plaintiff's complaint must be taken as admitted *in the procedural posture of that case.* Once again, however, the defendant made no effort to show that the jurisdictional allegations were untrue. In fact, as far as can be determined from the opinion, the defendant never moved to dismiss for lack of jurisdiction.

Thus, none of the cases cited by the Fifth Circuit in its opinion are in any way dispositive of the issue presented in the instant cause of action, since in none of the above cases, did the defendant attack the truth of plaintiff's jurisdictional allegations. The instant case does not fall in this category, because Petitioners have shown by evidence that the Respondent's jurisdictional allegations are untrue, and it is on that basis that they contend no subject matter jurisdiction exists.

This second type of Rule 12(b)(1) motion, which asks the trial court to go behind the allegations to determine the actual facts, has been sanctioned as proper by the Supreme Court and by the Third, Fourth, Sixth and Tenth Circuits. The Fifth Circuit should not be allowed to reach a contrary result, especially when such result has been reached because of a failure to differentiate between the nature of motions filed under Rule 12(b) (1).

The position which the Fifth Circuit has taken renders Rule 12(b)(1) virtually meaningless. If a plaintiff can maintain jurisdiction by allegations alone even though the defendant is able to prove that such allegations are entirely false, then the requirements for federal jurisdiction have become mere formalities which can be sattisfied by ritual genuflections and empty verbiage. No plaintiff with a competent attorney would ever find his case dismissed for lack of jurisdiction and the overcrowded federal courts would become still more crowded. Such a result is neither desirable from a policy viewpoint nor would it lead to more equitable results.

In the instant cause of action, the District Court considered lengthy affidavits and numerous exhibits. It listened to extensive oral argument from counsel, and when it asked counsel for both sides if an evidentiary hearing was needed, both counsel answerd in the negative. After studying all the evidence before it, the trial court, consistent with the great weight of authority, concluded that the plaintiff's allegations were false and that jurisdiction did not exist. The Fifth Circuit's reversal will render every case alleging jurisdiction to be sacrosanct until the case is tried on its merits, thus effectively eliminating Rule 12(b)(1).

Since jurisdiction must be decided by the court and can not be determined by a jury, the result of the Fifth Circuit's opinion is that at the time of trial the District Court will once again determine the same issue largely on the evidence which it has already had before it. It may well reach the same decision at that point, but not until many months have passed and thousands of dollars have gone to waste.

The Fifth Circuit, by its decision, has taken away from its district courts a power which they always had possessed. At a time when the federal courts are staggering under an increasingly heavy burden of cases, a policy which permits

causes of action to remain in the federal courts even when the allegations which placed them there in the first place have been found to be untrue by a District Court after a full hearing and with a full supporting record, is a grievous waste of scarce judicial resources. Moreover, it places a heavy burden both as to time and expense on the Petitioners at a time when it is not even clear that they are properly before the court in the first place. As the court remarked in *Hilton* v. *W. T. Grant Co.*, 212 F.Supp. 126 (W.D.Pa., 1962) at 130:

> "It is also true that, just as taxation is one of the inescapable burdens of life in a civilized society . . . so is the necessity of defending unmeritorious litigation. . . . No method has yet been devised for escaping these burdens; but the burdens incident to the status of a defendant ought not to be augmented until it is certain that the party involved really is properly a defendant."

CONCLUSION

Petitioners submit that their Writ of Certiorari should be granted for three reasons. First, the Fifth Circuit dismissed the trial court's finding that the transaction which is the basis of this lawsuit was not a "sale" within the meaning of the Securities Act merely by observing that the transaction complained of fell within the literal definition of a "sale". However, the Supreme Court's decisions in *United Housing Foundation, Inc.* v. *Forman* and *Kern County Land Co.* v. *Occidental Petroleum Corp.* make it clear that this is not a proper standard to apply to determine whether a transaction falls within the Securities Acts, and that instead the Fifth Circuit should have looked at the economic realities of the transactions involved.

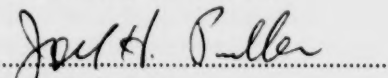
Second, the Fifth Circuit agreed with the district court's finding that this law suit arose out of a divorce property

settlement. Nevertheless, without discussion, it concluded that the Federal Securities laws apply to divorce property settlements. By so holding, the Fifth Circuit thrust the federal courts into the field of divorce and domestic relations. The Supreme Court and other federal courts have reiterated for more than a century that this field is an area in which the state courts have exclusive jurisdiction and the federal courts have none.

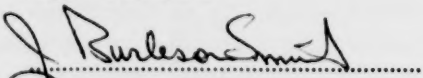
Third, the Fifth Circuit decided this case operating under the rule that when a motion to dismiss for lack of subject matter jurisdiction is heard, the jurisdictional allegations in a plaintiff's complaint must be taken as true. However, this is not the rule and has never been the rule in those instances where the defendant has challenged the truth of the jurisdictional allegations in the plaintiff's complaint. The Fifth Circuit's holding flatly contradicts and conflicts with decisions of the Supreme Court and the Third, Fourth, Sixth and Tenth Circuit Courts of Appeals.

For each of these reasons, the Supreme Court should grant Petitioners' Writ of Certiorari, and place this case on its calendar for oral argument.

Respectfully submitted,



JOEL H. PULLEN



J. BURLESON SMITH

CHARLES M. JEFFERSON

Attorneys for Petitioners

CERTIFICATE OF SERVICE

I, JOEL H. PULLEN, do hereby certify that true and correct copies of the foregoing Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit have been mailed to Lang, Cross, Ladon, Boldrick & Green, Attorneys at Law, 1565 Frost Bank Tower, San Antonio, Texas 78205, and Mitchell & Stewart, Attorneys at Law, 1540 Milam Building, San Antonio, Texas, 78205, counsel for Respondent herein, on this the 10th day of November, 1975.

Joel H. Pullen

JOEL H. PULLEN

ARCHIVE

APPENDIX A

pp. 1a - 19a

BERNARD D. SPECTOR,
Plaintiff-Appellant,

v.

L Q MOTOR INNS, INC., *et al.*,
Defendants-Appellees.

No. 74-2549.

UNITED STATES COURT OF APPEALS,
FIFTH CIRCUIT.

Aug. 8, 1975.

Husband who had received stock, which had been registered in his wife's name, in connection with property settlement, who had sold the stock back to the corporation after receiving assurances from the incorporators, one of whom was his wife, that the corporation's stock was not to be offered to the public, brought action against the incorporators and a successor corporation after the original corporation's assets had been transferred to the successor corporation and that corporation's stock had been offered to the public. The District Court for the Western District of Texas, John H. Wood, Jr., J., dismissed for lack of jurisdiction under the Securities Exchange Act, and husband appealed. The District Court, Gibson, Circuit Judge of the Eighth Circuit, sitting by designation, held that husband's allegations that incorporators had misrepresented to him their intention as to a public offering and that the public offering had brought a higher price for the stock in the successor corporation than husband had been paid for his stock was sufficient to allege the existence of a "sale" within meaning of the Securities Exchange Act and to state a claim within the jurisdiction of the Act.

Reversed and remanded.

1. Courts (Key) 486.5(6)

On appeal from dismissal for lack of jurisdiction, well pleaded allegations of the complaint must be taken as true.

2. Courts (Key) 406.1(11)

In reviewing dismissal of complaint for lack of jurisdiction under the Securities Exchange Act, court is limited to observing whether the complaint is drawn to seek recovery under the federal statute and, if so, determining whether, as a matter of law, the federal claim clearly appears to be immaterial and made solely for the purpose of obtaining jurisdiction or is wholly insubstantial and frivolous. Securities Exchange Act of 1934, § 27, 15 U.S.C.A. § 78aa.

3. Courts (Key) 299.3(1)

Jurisdiction is not defeated by the possibility that the averments might fail to state a cause of action or because the plaintiff might be unable to prove his case; such failures call for dismissal on the merits, not on jurisdictional grounds.

4. Courts (Key) 489(1)

Although divorce and its attendant property settlement are controlled by state law, husband's securities fraud claim against former wife and other incorporators of corporation, stock of whose predecessor husband received as part of property settlement, fell within subject matter jurisdiction of federal courts. Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b).

5. Courts (Key) 289(6)

Where husband brought action against former wife and other incorporators of corporation, stock of whose predecessor husband had received as part of property settlement, fact that the action might be barred by collateral estoppel impact of facts adjudicated in the divorce settlement did not demonstrate lack of jurisdiction in federal court under the Securities Exchange Act. Securities Exchange Act of 1934, §§ 10(b), 27, 15 U.S.C.A. §§ 78j(b), 78aa.

6. Federal Civil Procedure (Key) 1951

In action brought by husband against former wife and other incorporators of corporation based on alleged securities laws violations in connection with husband's sale of stock back to the corporation's predecessor, question of husband's entitlement to recover and question of federal court's jurisdiction over the transaction as a "sale" under the Securities Exchange Act were factually meshed and district court should have considered the merits of the controversy in a plenary hearing in order to insure a proper determination of jurisdiction; decision on the merits should have been reserved until a hearing on the merits. Securities Exchange Act of 1934, §§ 10(b), 27, 15 U.S.C.A. §§ 78j(b), 78aa; Fed.Rules Civ.Proc. rule 12(d), 28 U.S.C.A.

7. Securities Regulation (Key) 60

Husband's allegations that he received, in property settlement, shares of stock in corporation owned by his wife and others, that the stock had been community property registered in his wife's name, that he sold the stock back to the corporation, that the incorporators misled him by stating that they did not have any plans at that time to sell the stock to the public, and that the incorporators thereafter formed a new corporation with the assets of the old and

sold the stock to the public at a price in excess of that received by the husband stated a claim for violation of securities laws. Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b).

8. Courts (Key) 359.1(12)

Precise nature of husband's interest in 40 shares of stock registered in his wife's name was a matter governed by Texas property law.

9. Securities Regulation (Key) 43, 64

Husband's allegations that shares of stock registered in his wife's name were community property and that, before property settlement in which he received some of the shares, which he sold back to the corporation, he individually owned an interest in some of them, that he sold the shares back to the corporation upon assurances that the corporate stock was not to be the subject of public offering, and that the incorporators then transferred the assets of the corporation to a new corporation and offered stock in that corporation to the public at a price in excess of that paid to the husband alleged a "sale" of securities by the husband within meaning of Securities Exchange Act of 1934, §§ 3(a)(14), 10(b), 15 U.S.C.A. §§78c(a)(14), 78j(b).

See publication Words and Phrases for other judicial constructions and definitions.

10. Husband and Wife (Key) 262.1(1)

In community property state such as Texas, beneficial interests of husband and wife in community property are presumptively equal, whether nominal title is in the wife, in the husband, or in both jointly; if, during marriage, property is placed in the wife's name, only legal title vests

in her and equitable title to husband's one-half of the property remains in him.

11. Husband and Wife (Key) 272

Under Texas law, community property remains such unless formally partitioned in one spouse's name in accordance with Texas statutory law or unless transferred by gift from one spouse to the other.

12. Courts (Key) 299.3(2)

Husband who alleged that he had sold certain shares of stock to corporation upon assurances that corporation's stock would not be offerd to the public and that the corporaion's assets were thereafter transferred to another corporation whose stock was offered to the public and that he obtained a much lower price for his stock than was paid by the public adequately alleged injury in fact to give husband standing, within case or controversy requirement, to bring securities fraud action against the incorporators and the successor corporation. Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b); U.S.C.A. Const. art. 3, § 1 et seq.

13. Securities Regulation (Key) 64

Term "purchase or sale," as used in statute prohibiting use of deceptive and manipulative devices in connection with purchase or sale of securities, and as used in SEC rule relating to the same subject, is not limited to technical common-law sales. Securities Exchange Act of 1934, §§ 3(a)(14), 10(b), 15 U.S.C.A. §§ 78c(a)(14), 78j(b).

See publication Words and Phrases for other judicial constructions and definitions.

14. Securities Regulation (Key) 2

Terms of Securities Exchange Act are to be broadly construed to effectuate the Act's remedial purpose. Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b).

15. Securities Regulation (Key) 139

Husband who alleged that he had obtained shares of stock in corporation in connection with property settlement, that he had sold the shares back to the corporation after obtaining assurances that the corporation's stock was not to be offered to the public, that the incorporators, who included his former wife, thereafter transferred the assets of the corporation to a new corporation and offered successor corporation's stock to the public, and that he received less for his shares than the successor corporation received from the public sufficiently alleged fraud in connection with the sale of a security. Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b).

16. Securities Regulation (Key) 120

Husband who alleged that he had received stock, which had been registered in his wife's name, in connection with property settlement, that he had sold the stock back to the corporation, and that he had been misled by representations made when he sold the stock and thus received less than he should have was arguably within the zone of interest to be protected by the Securities Exchange Act and thus had standing to bring action against the incorporators. Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b); U.S.C.A.Const. art. 3, § 1 et seq.

17. Courts (Key) 489(1)

Availability of relief under Texas law did not deprive plaintiff of federal forum for his securities fraud action.

Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b).

Ernest J. Altgelt, III, James D. Stewart, San Antonio, Tex., for plaintiff-appellant.

Joel Pullen, J. Burleson Smith, San Antonio, Tex., for defendants-appellees.

Appeal from the United States District Court for the Western District of Texas.

Before GIBSON,* THORNBERRY and AINSWORTH, Circuit Judges.

GIBSON, Circuit Judge.

This fraud action involves a sale of securities used to fund a divorce property settlement between Bernard D. Spector, the plaintiff, and his wife. Violations of § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j (1970), SEC Rule 10b—5, 17 C.F.R. § 240.-10b—5 (1974), and pendent state claims[1] are alleged against L J Motor Inns, Inc., its controlling shareholder-directors, Samuel E. Barshop, Philip M. Barshop, and Norman S. Davis, and the plaintiff's former wife, Doris Barshop Spector. Jurisdiction is invoked under § 27 of the Securities Exchange Act of 1934, 15 U.S.C. § 78aa (1970).[2] Diversity of citizen-

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* Of the Eight Circuit, sitting by designation.

[1] As pendent claims Spector alleges state securities fraud, breach of fiduciary duty, common law fraud and unjust enrichment.

[2] The statute reads in part:

> The district courts of the United States * * * shall have exclusive jurisdiction of violations of this chapter [2B] or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this chapter or the rules and regulations thereunder.

ship is lacking, so federal jurisdiction rests solely upon the alleged Securities Act violation.

The plaintiff seeks $1,144,406 in damages plus attorney's fees. The defendants, without filing an answer, moved to dismiss for lack of jurisdiction. The District Court after a nonevidentiary hearing granted the motion on the basis that the alleged "sale" of securities was not "the type of transaction intended to be protected and covered" by § 10(b) and Rule 10b—5. We reverse and remand for a plenary hearing on the merits.

[1, 2] Since this is an appeal from dismissal for lack of jurisdiction, the well-pleaded allegations of the complaint must be taken as true. *Mindes* v. *Seaman,* 453 F.2d 197 (5th Cir. 1971); *Herpich* v. *Wallace,* 430 F.2d 792, 802 (5th Cir. 1970). Our review is limited to observing whether the complaint is drawn to seek recovery under a federal statute, and if so, determining whether as a matter of law the federal claim "clearly appears to be immaterial and made solely for the purpose of obtaining jurisdiction or * * * is wholly insubstantial and frivolous." *Bell* v. *Hood,* 327 U.S. 678, 682-83, 66 S.Ct. 773, 776, 90 L.Ed. 939 (1946). If not, dismissal for lack of jurisdiction was error. *Dann* v. *Studebaker-Packard Corp.,* 288 F.2d 201, 206 (6th Cir. 1961).

[3, 4] Jurisdiction is not defeated by the possibility that the averments might fail to state a cause of action or because the plaintiff is unable to prove his case. Such failures call for dismissal on the merits, not on jurisdictional grounds. *Bell* v. *Hood, supra* at 682, 66 S.Ct. 773. To be sure, this case presents a novel factual setting for a federal claim of securities fraud, as it arises out of a property settlement in a divorce action. Although the divorce and its attendant property settlement are controlled by state law, plaintiff's 10b—5 claim falls within the subject matter

jurisdiction of the federal courts. Whether plaintiff is entitled to relief depends upon a number of factual questions. The key issue appears to us to be whether plaintiff was the legal and equitable owner of the securities in question with full rights of disposal, unfettered by controlling restrictions on alienation.

The transaction urged as a basis for federal jurisdiction was a transfer of 18 shares of common stock by Spector as part of a divorce property settlement concluded with his wife in the District Court of Bexar County, Texas, March 16, 1972. Immediately after entry of the divorce decree the parties executed and exchanged some 20 documents prepared in advance by counsel for both sides which were the product of two years of negotiation that began in 1969 when Mrs. Spector filed for divorce.

The Spectors' community estate, itemized in the final settlement agreement, included 40 shares of common stock in Barshop Motel Enterprises, Inc. (BME), a privately held predecessor to defendant L Q Motor Inns, Inc., a publicly, held Delaware corporation operating a chain of 31 inns in southwestern states. BME was one of various business interests owned by Mrs. Spector's family, the Barshops. The certificate for the 40 shares of BME stock was registered in Mrs. Spector's name and constituted one-third of the outstanding capital stock of BME. From the start of the negotiations Spector claimed community ownership in the stock. In partial settlement of Spector's community property claims, he was issued a certificate for 18 of the 40 BME shares.[3] A stock purchase agreement was executed by BME contemporaneously, obliging Spector to immediately endorse the certificate back to BME in exchange

[3] The new certificate was dated March 14, 1972, two days before the divorce decree. It represented 15% ownership of the corporation.

for $70,000 cash and a secured promissory note in the amount of $300,000. Spector received other community assets and liabilities in the settlement as well, free of Mrs. Spector's claims.

Soon after BME purchased Spector's 18 shares, the defendants Barshop acquired the stock from BME for the same price, and in June, 1972, they incorporated as L Q Motor Inns, registered with the S.E.C., exchanged BME's assets for L Q stock and successfully sold L Q securities to the public. They acquired an equivalent 151,406 shares of L Q in exchange for the 18 BME shares purchased from Spector and in turn sold them publicly for $1,862,294.[4]

Plaintiff Spector alleged in his complaint, without mentioning the divorce, that during the negotiations for sale of his BME shares he inquired of BME's representatives (the defendants) "as to the current status of [BME's] efforts to effectuate a public sale of its securities." The defendants' response was that discussions with brokerage houses concerning public financing were under way but that there was "not presently in effect any contractual agreement for any such public financing."

BME's formal purchase agreement dated March 16, 1972, contained an express warranty to the same effect—disclaiming the existence of any present public financing contract.[5] The defendants inserted the warranty into the draft

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[4] Thus, in effect, the defendants bought the shares from plaintiff for the equivalent of $2.44 per share and sold them publicly at $12.30 per share. They were able as well to raise $615,000 for the corporation in the public offering.

[5] The BME stock purchase agreement drafted by BMS's counsel states in relevant part:

RECITALS

* * * * * *

[T]here have been discussions with various brokerage houses in the past concerning such public sale of securities and/or

agreement at the request of the plaintiff. Before they signed the warranty on March 16, 1972, however, plaintiff alleges, the defendants had already conducted "discussions, made plans, and [taken] steps to effectuate an exchange offer" in which a new corporation would be formed to acquire BME's assets and to sell securities to the public.[6]

As the basis for his claim of federal jurisdiction Spector argues that the transaction was a "sale" of securities and that the defendants in the March 16, 1972, agreement willfully concealed material facts—that the ultimately successful public offering had already been proposed and specific details discussed with the chosen underwriter. Disclosure of the proposed public sale, Spector argues, was necessary in the circumstances to prevent BME's statements from being misleading to him. And, had the defendants disclosed

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public financing and/or mergers with third parties and * * * such discussions are continuing and are expected to continue in the future, but BME has warranted to Spector that there is not presently in effect any contractual agreement for any such public financing * * * (Emphasis added.)

[6] The extent to which these plans were then finalized into a "public financing contract" are in dispute. In his brief on appeal to this court the plaintiff alleges that in June, 1971, three of the defendants met officers of E. F. Hutton & Co. concerning a public offering of securities of the chain of motels controlled by BME. After the conference a vice-president of E. F. Hutton's New York corporate underwriting department reportedly stated in a letter to BME:

> Based on what we know to date, it appears eminently reasonable to expect a highly successful offering for BME early in 1972 * *.

During the fall and winter of 1971, BME's counsel continued working on the proposed public offering with E. F. Hutton. On March 8, 1972, the week before BME purchased Spector's 18 shares, defendant Davis and a member of his law firm attended a conference in San Antonio between the Barshops and three officers of E F. Hutton. It was then agreed, plaintiff alleges, that a prospectus would be prepared and filed with the S.E.C. for a public offering of roughly 300,000 shares at approximately $15.00 per share.

their plans to him he would have "refused to sell his common stock, or any part thereof, at the price at which it was actually sold."

The only question now presented is whether the trial court erred in dismissing the suit for lack of jurisdiction without hearing the merits. Allegations of a violation of § 10(b) and Rule 10b–5 were made, but no proof was offered beyond the documents relating to the property settlement negotiations, divorce decree and L Q Motor Inns' public financing.[7] At the end of the hearing the court summarily dismissed the suit, finding that the plaintiff's cause of action grew out of an indivisible property settlement in the divorce action and concluding that the instant transaction was not of a type intended to be covered by the Act.[8] Plaintiff, of course, was still free to seek relief in the Texas courts.

[5] In support of dismissal, the defendants argue that the court lacks subject matter jurisdiction because no "sale" of securities took place. Spector, they argue, merely agreed to settle his community property claims against his wife in exchange for $400,000. The 18 shares of BME stock was used as a medium or device to supply $370,000 of the $400,000 settlement. The Barshops agreed (through BME) to issue Spector 18 shares of stock only for the purpose of purchasing it back from him immediately for $70,000 cash and a $300,000 note. At no time, they argue, did any "separate, independent negotiations [take place] which were

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[7] The documents included correspondence between Spector's counsel and counsel for Mrs. Spector (and BME) detailing the proposed property settlement, the settlement agreement itself, the judgment of divorce, the BME stock purchase agreement, the exchange offer and bill of sale transferring BME's assets to L Q Motor Inns, and L Q prospectus, memoranda to the court, and affidavits of defendants' counsel discussing the transaction.

[8] The court's May 7, 1974, memorandum opinion is unreported.

unrelated to the divorce suit based solely on a true purchase and sale of the BME shares." The stock purchase was simply "the means used to get this money to Spector."[9]

[6] The District Court, we believe, should have considered more extensively the merits of the controversy in a plenary hearing in order to insure a proper determination of jurisdiction. The jurisdictional and substantive issues are factually meshed. Therefore, decision on the jurisdictional issues is dependent on decision of the merits and should have been reserved until a hearing on the merits. *Land* v. *Dollar,* 330 U.S. 731, 67 S.Ct. 1009, 91 L.Ed. 1209 (1947); *McBeath* v. *Inter-American Citizens for Decency Committee,* 374 F.2d (5th Cir.), *cert. denied,* 389 U.S. 896, 88 S.Ct. 216, 19 L.Ed.2d 214 (1967). If the plaintiff prevails on his theory on the merits then he would also prevail on the jurisdictional issue. It is impossible to decide one without the other. *See also Gulf Oil Corp.* v. *Copp Paving Co.,* 419 U.S. 186, 213–14, 95 S.Ct. 392, 42 L.Ed.2d 378 n. 10 (1974)

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[9] In short, the defendants argue that the plaintiff is trying to cast his claim in 10b-5 terms because in that posture he has a "risk free shot" at improving his divorce settlement by more than one million dollars. That may be true, but to characterize the instant case as no more than a relitigation of the divorce action is to miss the point of Spector's complaint.

Hardy v. *Bankers Life & Cas. Co.,* 232 F.2d 205 (7th Cir.), *cert. denied,* 351 U.S. 984, 76 S.Ct. 1051, 100 L.Ed. 1498 (1956), upon which defendants rely, is inapposite here. It was a civil diversity action for conspiracy in which summary judgment was granted and affirmed upon res judicata grounds because the claim was foreclosed by a prior settlement in a state divorce proceeding involving substantially the same parties. The same claim of fraud was raised in the divorce action and rejected by the state court against the plaintiff. The instant case, however, is a 10b-5 claim dismissed on jurisdictional grounds involving issues not revealed by the record as having been litigated in the state divorce court. We intimate no view, however, of the possible collateral estoppal impact of facts adjudicated in the divorce settlement.

(Douglas, J., dissenting).[10] Such a procedure is authorized by Rule 12(d), Fed.R. Civ.P.

[7] Dismissal for failure to state a claim would also be inappropriate on the present record. It does not appear "to a certainty" that Spector would *not* be entitled to recover under any state of facts which could be proved in support of his claim. *Cook & Nichol, Inc.* v. *Plimsoll Club*, 451 F.2d 505, 506–07 (5th Cir. 1971). Moreover, because a decision on the merits in this case involves close factual questions of intent, reliance, and motive, along with legal questions on the significance of property rights recognized or created by the divorce settlement, summary judgment without a plenary hearing would be inappropriate. We do not suggest, however, that a directed verdict for the defendants might not be appropriate after all the evidence is in nor do we intimate any view on the merits of either party's position.

[8-11] That a sale of securities was alleged and can be proved by the plaintiff cannot be realistically disputed here. The precise nature of Spector's interest in the 40 BME shares registered in his wife's name is a matter governed by Texas property law and is not now before use. Suffice it to say, however, that the plaintiff has alleged facts which, with the documentary evidence before the District Court on the motion to dismiss, support a finding that the 40 shares were community property and that before the divorce settlement Spector individually owned an interest in at least some of them, notwithstanding that the shares were registered

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[10] *Cf. The Fair* v. *Kohler Die Co.*, 228 U.S. 22, 25, 33 S.Ct. 410, 412, 57 L.Ed. 716 (1913), in which Mr. Justice Holmes stated: [W]hen the plaintiff bases his cause of action .upon an act of Congress, jurisdiction cannot be defeated by a plea denying the merits of the claim. * * * [I]f the plaintiff really makes a substantial claim under an act of Congress, there is jurisdiction whether the claim ultimately be held good or bad.

in his wife's name.[11] Thus, at this early stage in the proceedings, plaintiff is entitled to an inference that at all relevant times, even before he property settlement, he owned an alienable interest in the BME stock. *See Hilley* v. *Hilley,* 342 S.W.2d 565, 568 (Tex.1961).

That Spector requested the defendants to insert the warranty into the BME stock purchase agreement to disclaim the existence of a public financing contract lends credibility to his claim of ownership. If Spector viewed his interest in the 18 shares as merely that of a pay-out conduit, as defendants argue, BME's future plans for financing would be of no concern to him. However, at this stage in the case we have no idea what the facts were. Thus, to dismiss the exchange of stock as merely part of an "indivisible" divorce settlement not cognizable under 10b-5 was premature. In the divorce settlement, of course, Spector's

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[11] In community property states such as Texas, the beneficial interests of husband and wife in community property are presumptively equal, whether nominal title is in the wife, husband or both jointly. Thus, if during marriage property is placed in the wife's name, only legal title vests in her and equitable title to the husband's one-half of the property remains in him. *Carter* v. *Barnes,* 16 S.W.2d 136, 139 (Tex.Civ.App.1929), *rev'd on other grounds,* 25 S.W.2d 606 (Tex.Comm.App.1930). Community property remains such unless formally partitioned in one spouse's name in accord with Texas statutory law, or unless transferred by gift from one spouse to the other. *Hilley* v. *Hilley,* 342 S.W.2d 565, 567-68, 571 (Tex.1961).

The instant record contains no findings of fact and scant evidence concerning the method by which Mrs. Spector acquired the certificate for 40 shares of BME stock — whether by gift, descent, or purchase with separate or community funds. Nor are there facts revealing any intent of the husband and wife that she would acquire the shares as her separate property, and no evidence of formal partition has been offered by the defendants to indicate such intent. On the contrary, there appears to be a judicial admission by the defendants and a similar decree by the Texas divorce court that Mr. and Mrs. Spector owned 40 shares as community property before the divorce and that Spector owned 18 shares free and clear of claims by his wife thereafter.

community property equity in BME was liquidated to 18 shares and a stock certificate was issued to him March 14, 1972. The contract of sale to BME was executed two days late, March 16, 1972, immediately after the property settlement was approved and the divorce decree entered in state court. To label this transaction a "sale" requires no strained construction of that term.[12]

We believe the issue presented here can better be framed as a question of standing to be decided within the framework of the case or controversy requirement of Article III of the Constitution. *Herpich* v. *Wallace,* 430 F.2d 792, 805 (5th Cir. 1970). In determining whether a 10b-5 plaintiff has standing to invoke the federal remedy:

> "[T]he first question is whether the plaintiff alleges that the challenged [conduct] has caused him injury in fact, economic or otherwise." The second question is whether "the interest sought to be protected by the complainant is arguably within the zone of interests to be protected" by section 10(b) and Rule 10b-5 thereunder.

Herpich v. *Wallace, supra* at 805 (citations omitted).

[12-16] The first question can be resolved easily. There is no doubt that Spector adequately alleged injury in fact. He claims he was deprived by the defendants of a reasonable opportunity to make an informed, intelligent decision regarding his sale of the securities and suffered a loss in

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[12] Section 3(a)(14) of the Act, 15 U.S.C. § 78c(a)(14) (1970), states:

Definitions and Application.

(a) *Definitions.*

When used in this chapter, unless the context otherwise requires —

• • • • • •

(14) The terms "sale" and "sell" each include any contract to sell or otherwise dispose of.

the sense of deprivation of a foreseeably more profitable sale had he known of the public financing plans.

The second question — whether the interest Spector seeks to protect is arguably within the zone of interests to be protected by the Act — reduces to whether the plaintiff has alleged with reasonable clarity that he sold securities that he had a right to sell, and that the sale was the subject of the fraudulent scheme or that the inducement of the sale was a purpose of the scheme. *Herpich* v. *Wallace, supra* at 808-09. The "purchase or sale" referred to in the statute and rule are not limited to technical common-law sales. *Dasho* v. *Susquehanna Corp.,* 380 F.2d 262 (7th Cir.), *cert. denied sub nom. Bard* v. *Dasho,* 389 U.S. 977, 88 S.Ct. 480, 19 L.Ed.2d 470 (1967); *see Hooper* v. *Mountain States Securities Corp.,* 282 F.2d 195 (5th Cir. 1960), *cert. denied,* 365 U.S. 814, 81 S.Ct. 695, 5 L.Ed.2d 693 (1961). The terms of the Act are to be broadly construed to effectuate its remedial purpose. *Tcherepnin* v. *Knight,* 389 U.S. 332, 88 S.Ct. 548, 19 L.Ed.2d 564 (1967). We conclude that the plaintiff has adequately alleged fraud in connection with a sale of securities.

[17] The availability of relief under Texas law does not deprive Spector of his federal forum. *Superintendent of Insurance* v. *Bankers Life & Casualty Co.,* 404 U.S. 6, 12, 92 S.Ct. 165, 30 L.Ed.2d 128 (1971). However, he must still prove his federal claim. We hold only that plaintiff must be gvien a chance to do so and that the court has jurisdiction to determine its jurisdiction by proceeding to a hearing on the merits.

The judgment of dismissal is reversed and the case remanded for further proceedings consistent with this opinion.

United States Court of Appeals

FOR THE FIFTH CIRCUIT

OCTOBER TERM, 1974

No. 74-2549

D. C. DOCKET NO. CA 73-285

BERNARD D. SPECTOR,
Plaintiff-Appellant,

v.

L Q MOTOR INNS, INC., ET AL.,
Defendants-Appellees.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF TEXAS

Before GIBSON,* THORNBERRY and AINSWORTH, Circuit Judges.

JUDGMENT

This cause came on to be heard on the transcript of the record from the United States District Court for the Western District of Texas, and was argued by counsel;

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, reversed; and that this cause be, and the same is hereby remanded to the said District Court for further proceedings consistent with the opinion of this Court;

It is further ordered that defendants-appellees pay to plaintiff-appellant, the costs on appeal to be taxed by the Clerk of this Court.

August 8, 1975

Issued as Mandate:

* Of the Eighth Circuit, sitting by designation.

United States Court of Appeals

FIFTH CIRCUIT

Office of the Clerk

October 3, 1975

TO ALL COUNSEL OF RECORD

No. 74-2549

Bernard D. Spector v. LQ Motor Inns, Inc., et al.

Dear Counsel:

This is to advise that an order has this day been entered denying the petition(x) for rehearing, and no member of the panel nor Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc (Rule 35, Federal Rules of Appellate Procedure; Local Fifth Circuit Rule 12) the petition(x) for rehearing en banc has also been denied.

See Rule 41, Federal Rules of Appellate Procedure for issuance and stay of the mandate.

Very truly yours,

EDWARD W. WADSWORTH,
Clerk

By CLARE F. SACHI ,
Deputy Clerk

cc: Mr. Ernest J. Altgelt, III
Mr. James D. Stewart
Mr. Joel Pullen
Mr. J. Burleson Smith

APPENDIX B

pp. 20a - 22a

IN THE
UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
SAN ANTONIO DIVISION

BERNARD D. SPECTOR

Plaintiff,

CA No. SA-73-CA-285

SAMUEL E. BARSHOP, PHILIP M. BARSHOP, DORIS BARSHOP SPECTOR, NORMAN S. DAVIS and L Q MOTOR INNS, INC.

Defendants.

MEMORANDUM AND ORDER DISMISSING CAUSE FOR LACK OF JURISDICTION

On the 24th day of April, 1974, came on to be heard Defendants' Motion to Dismiss this cause for lack of jurisdiction. All parties announced ready on the motion upon the record then before the Court.

Plaintiff's sole basis for Federal jurisdiction is alleged violations of Section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C.78j) and Rule 10(b)-5 promulgated thereunder by the Securities and Exchange Commission. In addition, Plaintiff alleges violations of the Texas securities laws, common law fraud and breach of fiduciary duties. These, of course, are based upon pendent jurisdiction and must be dismissed unless there is a viable Federal claim supporting jurisdiction in this Court.

After considering the pleadings, the record including the affidavits and other materials filed by the parties, and the briefs and argument of counsel, the Court found, and now finds, that:

1. Plaintiff's alleged causes of action grow out of an indivisible property settlement in a divorce action in which final judgment was entered in a Texas State Court of competent jurisdiction over divorce property settlements;

2. There were no separate independent negotiations concerning the value of any particular shares of stock involved in the divorce settlement, but, rather, the parties first agreed on a dollar amount which the Plaintiff here (the Defendant in the Divorce Action) would receive as his part of the partition of the property involved in the divorce settlement and then they agreed upon a method of realizing that dollar amount so determined. The method agreed upon by them prior to the entry of the divorce decree awarded to the Plaintiff here certain shares of stock which the Defendant Doris Barshop Spector was obligated to buy (or to provide a buyer) and which the Plaintiff here was obligated to transfer for an agreed consideration immediately after the entry of the divorce decree. This agreement made before the entry of the divorce decree was executed and consummated, as agreed, immediately after the entry of the divorce decree, which also approved the property settlement, all as a part of the overall agreement between the parties.

3. The Plaintiff here is attempting to re-open an indivisible property settlement without tendering what he received in the settlement or without having sought relief in the Texas State Court which entered the divorce decree and approved the property settlement; and

4. The Plaintiff can obtain all of the relief to which he is entitled in the Texas State Courts, and his counsel so conceded in open Court on oral argument.

Accordingly, the Court concludes (1) that this is not the type of transaction intended to be protected and covered by Section 10(b) and (2) that this Court has no jurisdiction over the alleged Federal cause of action. Accordingly, Defendants' Motion to Dismiss is granted as to all causes of action alleged in the Plaintiff's Complaint.

Entered this 7th day of May, 1974.

/s/ JOHN H. WOOD, JR.
John H. Wood, Jr.
United States District Judge

San Antonio, Texas
May 7, 1974

APPENDIX C

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Securities Exchange Act of 1934 — 15 § 78c

Definitions and application — Definitions

(a) When used in this chapter, unless the context otherwise requires —

(14) The terms "sale" and "sell" each include any contract to sell or otherwise dispose of.

Securities Exchange Act of 1934 — 15 § 78j

Manipulative and deceptive devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange —

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

S.E.C. Rule 17 C.F.R. 240.106-5. Employment of Manipulative and Deceptive Devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

Federal Rule of Civil Procedure 12(b)

Rule 12. Defenses and Objections — When and How Presented — By Pleading or Motion — Motion for Judgment on Pleadings

(b) How Presented. Every defense, in law or fact, to a claim for relief in any pleading, whether a claim, counterclaim, cross-claim, or third-party claim, shall be asserted in the responsive pleading thereto if one is required, except that the following defenses may at the option of the pleader be made by motion: (1) lack of jurisdiction over the subject matter, (2) lack of jurisdiction over the person, (3) improper venue, (4) insufficiency of process, (5) insufficiency of service of process, (6) failure to state a claim upon which relief can be granted, (7) failure to join an indispensable party. A motion making any of these defenses shall be made before pleading if a further pleading is permitted. No defense or objection is waived by being joined with one or more other defenses or objections in a responsive pleading or motion. If a pleading sets forth a claim for relief to which the adverse party is not required to serve a responsive pleading, he may assert at the trial any defense in law or fact to that claim for relief. If, on a motion asserting the defense numbered (6) to dismiss for failure of the pleading to state a claim upon which relief can be

granted, matters outside the pleading are presented to and not excluded by the court, the motion shall be treated as one for summary judgment and disposed of as provided in Rule 56, and all parties shall be given reasonable opportunity to present all material made pertinent to such a motion by Rule 56.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-688

L Q MOTOR INNS, INC., SAMUEL E. BARSHOP, PHILIP M. BARSHOP, DORIS BARSHOP SPECTOR AND NORMAN S. DAVIS,

Petitioners,

versus

BERNARD D. SPECTOR,

Respondent.

On a Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

RESPONDENT'S BRIEF IN OPPOSITION

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IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1975

No. 75-688

L Q MOTOR INNS, INC., SAMUEL E. BARSHOP, PHILIP M. BARSHOP, DORIS BARSHOP SPECTOR AND NORMAN S. DAVIS,
Petitioners,

versus

BERNARD D. SPECTOR,
Respondent.

On a Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

RESPONDENT'S BRIEF IN OPPOSITION

OPINIONS BELOW

The opinion of the Court of Appeals entered August 8, 1975 is reported at 517 F.2d 278 (Petitioners' Appendix A). The memorandum opinion of the District Court entered May 7, 1974 is unreported (Petitioners' Appendix B).

JURISDICTION

The jurisdictional requisites are adequately set forth in the Petition.

NATURE OF CASE

This litigation is concerned with a fraudulently induced sale of securities, which Respondent owned free and clear under a Texas divorce judgment. Respondent Bernard D. Spector alleges that Petitioners fraudulently induced him to sell 18 shares of stock in Barshop Motel Enterprises, Inc. ("B.M.E.") while wilfully concealing material facts as to an imminent public offering of such stock.

Without citing a single precedent, the District Court dismissed on the grounds that it had "no jurisdiction over the alleged cause of action." The Fifth Circuit reversed and remanded the cause for further proceedings, holding that the Respondent must be given a chance to prove his claim made under SEC Rule 10b-5, and that the trial court had jurisdiction to determine the jurisdictional and substantive issues.

QUESTION PRESENTED

This case presents but one issue not set forth in the Petition for Certiorari. That issue is:

> Whether in view of the verified amended complaint, affidavits, and documents presented, the Court of Appeals correctly held that Re-

spondent had not made a "wholly insubstantial and frivolous claim" under Section 10(b) of the Securities Exchange Act and SEC Rule 10b-5, the decision of which requires further proceedings on the merits so as to resolve factual disputes and to insure a proper determination of any jurisdictional issues.

This issue was discussed by the Court of Appeals in its opinion, and the controlling precedents clearly noted.

STATUTES AND RULES INVOLVED

The statutes and rules involved are set forth in Annex G, *infra*, beginning at page 43a. They include the following:

United States Constitution,
Article III, Section 2

Securities Exchange Act,
15 U.S.C. §§ 78c, 78j, 78aa

Exchange Act Rule 10b-5,
17 C.F.R. § 240.10b-5

Federal Rules of Civil Procedure,
Rules 8, 12 and 56

COUNTER-STATEMENT OF THE CASE

The facts of the case are stated in detail in the decision of the Court of Appeals (Petitioners' Appendix A).

As the Fifth Circuit observed, a final judicial determination of this controversy admittedly requires the resolution of a number of "factual questions" (517 F.2d at 282, 284).

Many of the statements and conclusions contained in Petitioners' "Factual Background" are either incorrect or subject to material factual disputes. We will not attempt to correct each of these misstatements.

Petitioners create the misimpression that Respondent Spector never had an ownership interest in the B.M.E. stock that was sold. However, the Property Settlement Agreement and Judgment of Divorce awarded 18 shares of B.M.E. stock to Respondent as his sole and separate property, free and clear. (Annex C and D, *infra*) Further, as Chief Judge Gibson noted, there is ample evidence in the record reflecting that Respondent and his wife owned 40 shares of B.M.E. stock as community property before the divorce (517 F.2d at 284-285). In Annex B, C, D and F, *infra*, portions of certain documents supporting this contention are underlined in red.

Petitioners create the misimpression that the Judgment of Divorce and the Property Settlement Agreement approved by the divorce court required Respondent Spector to sell his stock in B.M.E. However, nothing in these documents required such a sale. (See Annex C and D, *infra)* Affidavits filed establish that the stock sale was not part of the property settlement between husband and wife, but was a sale to B.M.E., which was an entity entirely separate and distinct

from either party to the divorce (App. 271-275)[1]. B.M.E.'s purchase of Respondent's stock was a "separate transaction founded upon a written instrument . . . to be executed *only after* the final Judgment of Divorce had been entered." (App. 272; see also Annex B, *infra* at pp. 16a-21a)

Even the fee statement and opinion letter rendered by the lawyers in connection with the agreement for B.M.E.'s purchase of Respondent's stock were addressed to B.M.E., not to Respondent's ex-wife. (App. 273-274, 279-281).

In short, the record reveals a number of material "factual disputes" foreclosing dismissal of this suit prior to a trial on the merits. Annex A, *infra*, is a table giving a partial list of these factual disputes which oppose many of the statements made in the "Factual Background" of the Petition.

ARGUMENT

The three "Questions Presented" listed in the Petition are dealt with in the same order below under Points I, II, and III. None of Petitioners' three questions are presented for review; but instead such questions have been propounded in an attempt to have the Court prematurely determine spurious legal issues, premised upon false or disputed factual assumptions.

---

1 The term "App." refers to the printed Appendix as filed with the Fifth Circuit. A copy of such Appendix as well as the briefs filed with the Fifth Circuit have been certified to the Court pursuant to U.S. Supreme Court Rule 21.

I

The Decision Of *United Housing Foundation v. Forman*, ___ U.S. ___, 95 S.Ct. 2051, 44 L. Ed. 2d 621 (1975) Has No Application To What Is At Issue Herein

Petitioners argue that the Fifth Circuit's opinion is in error in light of the Court's decision in *United Housing Foundation v. Forman*, ___U.S. ___, 95 S. Ct. 2051, 44 L. Ed. 2d 621 (1975). Despite the suggestion at pages 12 and 18 in the Petition to the contrary, the *United Housing Foundation* case was specifically cited to the Fifth Circuit prior to its decision on August 8, 1975. In a letter dated June 23, 1975 addressed to the Fifth Circuit, Petitioners specifically sent to Circuit Judges Gibson, Thornberry and Ainsworth copies of the *United Housing Foundation* decision. In their motion for rehearing and rehearing en banc, moreover, Petitioners unsuccessfully reurged the applicability of the *United Housing Foundation* decision.

The Fifth Circuit correctly decided that *United Housing Foundation* does not apply to our case. The holding in that case was that "so-called" shares of stock issued by a massive housing co-operative were not "securities" within the meaning of Section 2(1) of the Securities Act of 1933 [15 U.S.C. §77b(1)]. In reaching that result, the Court reasoned that the so-called "shares" were not bought in hopes of receiving profits from the efforts of others, but were bought to provide living quarters for themselves.

In our case, the stock sold by Respondent to Petitioners was in a corporation operating a chain of 33 motels so that investors such as Spector had a reasonable expectation of making profit from the efforts of others.

The rejection by the Fifth Circuit of the decision in *Kern County Land Co. v. Occidental Petroleum Corp.*, 411 U.S. 582 (1973) was also correct. That litigation pertained to a suit brought under Section 16(b) of the Securities Exchange Act that involved a situation where the transaction complained of was the execution of a stock option agreement by the owner of more than 10% of the shares in connection with a blocked tender offer. A divided Court, after reviewing the transaction complained of, held that the short swing profit prohibitions of Section 16(b) had not been violated because "The option . . . does not appear to have been an instrument with potential for speculative abuse . . ." 411 U.S. at 602. In short, there was no "sale" because there had not been any "exploitation of inside information". *Id.* at 603.

In our action, Respondent Spector alleges that there has been *fraudulent conduct and the wilful concealment of material inside information* (Annex B, *infra*). To adopt Petitioners' position would be to deprive any divorced person of the protection of "full disclosure" as afforded by the federal securities laws in selling securities obtained in divorce proceedings "free from any claim" (Annex B, at p. 16a; Annex C, at pp. 25a, 28a).

The verified allegations made in the First Amended Complaint as well as the affidavits and other evidence

in the record show an archetypal 10b-5 case involving the "purchase by one group in a closed corporation of the interest of another, without disclosing negotiations for the sale or disposition of the issuer's assets or its securities at a higher price." 1 Bromberg, *Securities Law: Fraud-SEC Rule 10b-5*, §4.2 at p. 70 (1974). In this connection, Respondent asserts:

(1) that Petitioners caused a closed corporation to purchase 18 shares of stock for $370,000.00;
(2) that Petitioners in connection with B.M.E.'s purchase of Spector's stock utilized materially false and misleading statements;
(3) that Petitioners wilfully concealed from Spector material facts about a proposed "public offering" through E. F. Hutton & Company, Inc.; and
(4) that Respondent would have refused to sell his shares of common stock, or any part thereof, for $370,000.00 if disclosures had been made as to the E. F. Hutton public offering.

Under facts substantially similar to those involved herein, the courts have uniformly held that there is jurisdiction under Section 10(b) of the Securities Exchange Act and SEC Rule 10b-5. *Rochez Bros., Inc. v. Rhoades*, 491 F.2d 402 (3rd Cir. 1974) — SEC Rule 10b-5 violated where co-owner of closed corporation in buying out other 50% owner failed to disclose his retention of a representative to find a purchaser for the entire corporation and his interview with two prospective

buyers; *Ross v. Licht*, 263 F. Supp. 395 (S.D.N.Y. 1967) — Persons who sold their stock in closed corporation for $120.00 a share were permitted to proceed under SEC Rule 10b-5 upon allegations that defendants had failed to disclose a proposed public offering of such stock for $600.00 a share; *Kardon v. National Gypsum Co.*, 69 F. Supp. 512 (E.D. Pa. 1946), subseq. opinions 73 F. Supp. 798 (E.D. Pa 1947) (on merits), 83 F. Supp. 613 (E.D. Pa 1947) (conclusions of law) — SEC Rule 10b-5 applicable where two brothers had bought securities sold by father and son for $504,000 without disclosing an agreement to sell closed corporation for $1,500,000; *Thomas v. Duralite Company*, 386 F. Supp. 698 (D. NJ 1974), liability aff'd CCH Fed. Sec. L. Rep. ¶ 95,322 [current] (3rd Cir. 1975) — SEC Rule 10b-5 violated where owner of 45 1/2% of the stock in a closely held corporation was induced to sell his stock to corporation by misrepresentations and nondisclosures about the improvement of the corporation's financial health and the possibility of a take over by a competitor; *Schine v. Schine*, 250 F. Supp. 822 (S.D. N.Y. 1966) subseq. opinion 254 F. Supp. 966 (S.D. N.Y. 1966), appeal dism'd 367 F.2d 685 (2nd Cir. 1966) — Subject matter jurisdiction upheld under SEC Rule 10b-5 where owner of 37.6% interest in family owned corporation was fraudulently induced by majority owners to sell stock at far less than actual value; *Robinson v. Difford*, 92 F. Supp. 145 (E.D. Pa 1950) — Jurisdiction upheld under SEC Rule 10b-5 where 1/3 owners of closely held corporation alleged they were fraudulently induced by misrepresentations to sell their shares to the defendant majority shareholders for substantially less than their true value. See also generally: Loss, Securities

Regulation, Vol. III at pp. 1466-1467 (1961); Vol. VI at p. 3613 (1969); 1 Bromberg, *supra* §4.2 (1970); Latty, *The Aggrieved Buyer or Seller or Holder of Securities in a closed corporation Under SEC Statutes*, 19 Law & Contemp. Prob. 505 (1953).

Chief Judge Gibson, therefore, was correct when he remarked that to label the transaction in our case a securities "sale" within the meaning of Section 3(a)(14) of the Exchange Act "requires no strained construction of that term." (517 F.2d at 285).

II

The Real Issue Is Not Whether Federal Courts Have Jurisdiction Over Divorce Property Settlements, But Whether Persons Who Sell Securities To Third Parties After The Judicial Dissolution Of Marriages Are Entitled To The Protections Of The Anti-Fraud Provisions Of SEC Rule 10b-5

In plain terms, this litigation amounts to an attempt by Respondent Spector to set aside a sale transaction wherein Petitioners realized proceeds of $1,862,294.00 directly traceable to the 18 shares of B.M.E. stock which were fraudulently acquired from him for only $370,000.00. The divorce judgment awarded Respondent these 18 shares of stock. Respondent does not request any modification of the divorce judgment.

Since we are in agreement that Federal Courts do not generally have jurisdiction over divorce matters, it is

not necessary to discuss the cases relied upon by Petitioners in support of this thesis.[2] Petitioners are in error, however, in the characterization of the Fifth Circuit's decision as permitting Respondent to "relitigate" his property settlement, thereby opening a "Pandora's box by vastly expanding the scope of the Federal Securities Law." (Petition at p. 23). Respondent obviously does not desire to set aside, relitigate, or modify so much as a single word or comma of the Property Settlement or Judgment of Divorce. In fact, Respondent Spector relies upon these very instruments as constituting an admission and judicial pronouncement that he at all relevant times was a minority shareholder of B.M.E. to whom its directors, controlling persons, officers, and successors owed fiduciary duties. See in this connection Count III of the verified First Amended Complaint, Annex B, *infra*; as well as the discussion in the Fifth Circuit's opinion at 517 F.2d 284-285, and in particular n. 11. Before the divorce, Respondent owned his community property interest in 40 shares; after the divorce, he owned 18 shares separately. (Annex C, D and F) No amount of

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2 *McCarty v. Hollis*, 120 F.2d 540 (10th Cir. 1941); *Druen v. Druen*, 247 F. Supp. 754, 755 (D. Colo. 1965); *Lutsky v. Lutsky*, 310 F. Supp. 517 (S.D. Fla. 1970); *Gargallo v. Gargallo*, 472 F.2d 1219 (6th Cir. 1973); *Shiffman v. Askew*, 359 F. Supp. 1225 (M.D. Fla. 1973), each merely follow the general rule that Federal Courts do not entertain actions involving matrimonial status or other domestic relations matters. Respondent seeks no such relief. See also: Wright, Law of Federal Courts 62, 285-286 (2d Ed. 1970). Here, of course, Respondent does not seek to attack, modify, or set aside the Property Settlement or Judgment of Divorce wherein he was awarded 18 shares of BME Stock as his sole and separate property without a requirement for a subsequent sale to anyone. This was fully discussed in Respondent's Memorandum of Law in Opposition to Motion to Dismiss for Lack of Jurisdiction. [App. pp. 227-233] Similarly *Spears v. Spears*, 162 F.2d 345 (6th Cir. 1947) cert. denied 332 U.S. 768 has no application where no construction or modification is requested of the Property Settlement or Divorce Decree.

strained rhetoric can change the simple truth that Respondent Spector is not challenging the fairness of the Property Settlement Agreement and Judgment of Divorce, wherein he was awarded 18 shares of stock "free of any claim." The Fifth Circuit's opinion is in no manner a precedent for modifying divorce judgments.

Respondent's complaint is against the officers, directors, and controlling persons of B.M.E., and its successor corporation L Q Motor Inns, Inc. It is these parties who combined and conspired and aided and abetted each other to accomplish a stock fraud involving a sum in excess of $1,000,000.00. Quite significantly, Petitioners have yet to file an answer or any affidavit from a party defendant in which a denial is contained to the verified allegations of fraudulent conduct by these parties.

III

There Is No Conflict Of Decisions As The Teaching Of *Bell v. Hood*, 327 U.S. 678 (1946) Is Applicable To Petitioners' Motion To Dismiss

The Fifth Circuit was entirely correct in its determination that for purposes of ruling upon Petitioners' motion to dismiss for lack of jurisdiction:

> Our review is limited to observing whether the complaint is drawn to seek recovery under a federal statute, and if so, determining whether as a matter of law the federal claim "clearly appears to be immaterial and made solely for

the purpose of obtaining jurisdiction or * * * is wholly insubstantial and frivolous." 517 F.2d at 281, citing *Bell v. Hood*, 327 U.S. 678, 682-683 (1946).

The motion to dismiss for lack of jurisdiction was not made on the merits, as Petitioners have now claimed again after having unsuccessfully urged this contention with the same supporting authorities before the Fifth Circuit. Quite to the contrary, Petitioners' motion to dismiss was made and heard by the District Court at the very commencement of the proceedings — without Petitioners ever having filed an answer — and without Petitioners having filed a single affidavit from a party-defendant to deny the verified allegations of fraudulent nondisclosures.[3]

There is ample precedent to the effect that under such circumstances the so-called "well pleaded complaint rule" must be followed; and the complaint is not dismissed unless the alleged claim under federal law was "so attenuated and unsubstantial as to be absolutely devoid of merit," *Newburyport Water Company v. Newburyport*, 193 U.S. 561, 579 (1904), or

3 Petitioners now argue that their motion was not designed to test the formal sufficiency of the allegations of the complaint by challenging "the truth of the jurisdictional allegations . . ." (Petition at p. 31). In the District Court Petitioners had not acknowledged the formal sufficiency of the allegations in the complaint. This is shown by the fact that Petitioners previously had filed a motion to dismiss the complaint under Rule 9(b), and 12(e), on grounds that the fraud had not been alleged with sufficient particularity (Rec. Doc. 8). On April 24, 1974 the District Court after considering said motion to dismiss stated "I'm going to overrule the motion for a more definite statement." [App. p. 459] Thus, in the District Court at the April 24th hearing Petitioners apparently were contesting the sufficiency of the complaint in both their motions to dismiss.

"frivolous," *Bell v. Hood, supra* at 683. Reference is made in this connection to the Court's decisions in: *Hart v. B. F. Keith Vaudeville Exchange*, 262 U.S. 271, 273-274 (1923); *Baker v. Carr*, 369 U.S. 186, 199 (1962); *Oneida Indian Nation of New York State v. County of Oneida, N. Y.*, 414 U.S. 661, 666-667, 676 (1974); *The Fair v. Kohler Die & Specialty*, 228 U.S. 22, 25 (1913); *Montana-Dakota Utilities Co. v. North-Western Public Service Co.*, 341 U.S. 246, 249 (1951); and generally see: Wright, Law of Federal Courts 62, 285-286 (2d Ed. 1970); 2A *Moore's Federal Practice* ¶ 8.09 (1974); 5 Wright & Miller, *Federal Practice and Procedure: Civil* § 1209 (1969).

The principle of *Bell v. Hood, supra* is fully applicable to cases brought under the Securities Exchange Act. *Dann v. Studebaker-Packard Corporation*, 288 F.2d 201, 206 (6th Cir. 1961) involved an action brought under the Securities Exchange Act wherein the defendants had moved to dismiss under Civil Rule 12(b)(1) for lack of subject matter jurisdiction. In overruling a District Court's dismissal, the Sixth Circuit commented:

> [I]t should be noted at this juncture that jurisdiction to consider the allegations of the complaint does not necessarily mean that such allegations, if established, will state a claim for the relief demanded under federal law, or, indeed, for any relief at all. In *Bell v. Hood*, 1946, 327 U.S. 678, 682, 66 S. Ct. 773, 776, 90 L. Ed. 939, the United States Supreme Court held:

> "Jurisdiction, therefore, is not defeated * * * by the possibility that the averments might fail to state a cause of action on which the petitioners could actually recover. For it is well settled that the failure to state a proper cause of action calls for a judgment on the merits and not for a dismissal for want of jurisdiction. Whether the complaint states a cause of action on which relief could be granted is a question of law and * * * must be decided after * * * the Court has assumed jurisdiction over the controversy."
>
> To say federal courts have jurisdiction of the subject matter herein, therefore, means merely that they may *consider* the merits of any federal question involved. Therefore, a dismissal at this stage on the broad ground of lack of jurisdiction of the controversy would be improper. 288 F. 2d. at 206.

Federal courts when faced with the contention that a securities transaction was not a "sale" within the meaning of Federal Securities Laws, such as was made by Petitioners in their motion to dismiss, have repeatedly followed the teaching of *Bell v. Hood, supra*. In this connection the Court is directed to the following: *Superintendent of Insurance v. Banker's Life & Casualty*, 300 F. Supp. 1083 (S.D.N.Y. 1969) aff'd 430 F.2d 355 (2nd Cir. 1970) rev'd 404 U.S. 6 (1971) — District Court dismissed because plaintiff was neither "purchaser" or "seller" of securities, the Second Circuit affirmed, and this Court reversed stating that

"this case must be remanded for a full trial"; *Hooper v. Mountain States Securities Corp.*, 282 F.2d 195, 199 (5th Cir. 1960), cert. denied 365 U.S. 814 (1961) — District Court dismissed because there was no "seller" or "purchaser", Fifth Circuit held that the well pleaded allegations must be taken as true and reversed citing *Conley v. Gibson*, 355 U.S. 41 (1957); *Coffee v. Permian Corp.*, 306 F. Supp. 1371 (N.D. Tex. 1969) rev'd 434 F.2d 383 (5th Cir. 1970) — District Court dismissed complaint because plaintiff had not participated in the "purchase" of any security, Fifth Circuit reversed because the complaint had sufficiently stated a claim under the Federal Securities laws; *A. T. Brod & Co. v. Perlow*, 375 F.2d 393, 396, 398 (2d. Cir. 1967) — District Court had dismissed for lack of subject matter jurisdiction because no fraud was alleged "usually associated with the sale or purchase of securities", Second Circuit reversed holding that it is clear that the complaint sufficiently stated a claim grounded in federal jurisdiction.

Nothing could be more misleading or incorrect than Petitioners' statement that the Fifth Circuit's decision "flatly contradicts earlier rulings of the Supreme Court and four other Courts of Appeal" (Petition at p. 24). All of Petitioners' authorities have little to do with the traditional, or "first type", Civil Rule 12(b)(1) motion, which was the motion filed in this action. We have, accordingly, consigned to the margin below our discussion of Petitioners' cases.[4]

4 *McNutt v. General Motors Acceptance Corporation*, 298 U.S. 178 (1936) involved a situation in which the plaintiff failed to allege any "facts" in his petition or introduce any evidence to support his general allegation to the effect that the amount in controversy exceeded $3000, the required jurisdictional amount. In our case, Respondent has alleged with particularity in his verified com-

Petitioners now admit that the First Amended Complaint alleges a good cause of action showing jurisdiction under the Securities Exchange Act; but then they somehow claim that when one "goes beyond the pleadings", some failure of jurisdiction is established.

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plaint the requisite jurisdictional facts. In addition Respondent fully informed Petitioners as well as the District Court that he "must be afforded full discovery to develop complete information as to the jurisdictional issues and is not required to try such issues upon affidavits". App. pp. 226-227; see also: App. pp. 460, 495-496, 506.

Gibbs v. Buck, 307 U.S. 66 (1939) involved an injunction suit brought under the copyright act. The defendants moved to dismiss because of the absence of the jurisdictional amount in that the loss of any member of the plaintiff society would not meet the jurisdictional requirements. The Court upheld the District Court's conclusion that the necessary jurisdictional facts had been adequately alleged and presented.

Local 336, American Federation of Musicians, AFL-CIO v. Bonatz, 475 F.2d 433 (3rd Cir. 1973) involved the suit brought by a musicians' union and leader against the proprietor of a cocktail lounge seeking to enforce arbitration award. The District Court *sua sponte* at a hearing upon the plaintiff's motion for a summary judgment dismissed the action upon jurisdictional grounds. The Third Circuit reversed the dismissal because the plaintiffs had not been given an adequate opportunity to establish the jurisdictional facts. In our case, Respondent similarly seeks the "right to take depositions," and to engage in further discovery to fully establish the jurisdictional facts. App. pp. 460, 226-227, 495-496, 506.

Prairie Band of Pottawatomie Tribe of Indians v. Puckkee, 321 F.2d 767 (10th Cir. 1963) was a declaratory judgment action to determine the rights of certain indians to congressionally appropriated funds. The Tenth Circuit affirmed the trial court's dismissal for lack of jurisdiction in that "this suit does not purport to invoke the construction and effect of the federal statute . . . ." In our case, the construction and effect of the Securities Exchange Act and SEC Rule 10b-5 promulgated thereunder is clearly involved. Annex B, *infra* at pp. 2a-9a.

Shahmoon Industries, Inc. v. Imperato, 338 F.2d 449 (3rd Cir. 1964) was a diversity action brought for a breach of fiduciary duty. Upon a jurisdictional point being raised for the first time in the appellate court, the Third Circuit reversed the judgment of the trial court and directed that further proceedings be held.

Spears v. Spears, 162 F.2d 345 (6th Cir. 1947) cert. denied 332 U.S. 768 is discussed in n. 2, *supra*.)

There was considerable confusion in the trial court as to whether Petitioner moved to dismiss for lack of subject matter jurisdiction under Rule 12(b)(1), or for failure to state a claim under Rule 12(b)(6), or for summary judgment under Rule 56. (App. pp. 494-497) The Fifth Circuit found that in each of these cases the motion should be denied, because of the fact issues that remain (517 F.2d at 284; Annex A, *infra*).

When one does go beyond the pleadings to look at the affidavits and other instruments, there is no way whatsoever that one can say that Respondent Spector "would *not* be entitled to recover under any state of facts which could be proved in support of his claim." 517 F.2d at 284; *Conley v. Gibson*, 355 U.S. 41, 45-46 (1957); *Herpich v. Wallace*, 430 F.2d 792, 802 (5th Cir. 1970). Affidavits and documents establish that Respondent Spector owned the stock that was sold to B.M.E. [Annex A, B, C, D and F; App. pp. 269-279]. The Property Settlement Agreement recites that Respondent owned stock interests at all times — community property before the divorce judgment and as separate property thereafter [Annex C]. The Judgment of Divorce approved the Property Settlement Agreement and awarded the 18 shares of B.M.E. stock to Respondent [Annex D].

Not only do the pleadings allege that Respondent had stock interests to sell, but also the rest of the record in fact establishes this conclusively.

IV

It Would Be Inadvisible To Grant Certiorari In View Of The Interlocutory Nature Of The Judgment Of The Court Of Appeals

As stated in *American Construction v. Jacksonville*, 148 U.S. 372, 384 (1893):

> [T]his Court should not issue a writ of *certiorari* to review a decree of the Circuit Court of Appeals on appeal of an interlocutory order, unless it is necessary to prevent extraordinary inconvenience and embarrassment in the conduct of the cause.

This reasoning fully applies to situations where the decision of the Court of Appeals sought to be reviewed is interlocutory in nature, such as where a cause is remanded to the District Court for further proceedings on the merits. *Brotherhood of Locomotive Firemen & Enginemen v. Bangor A. R. Co.*, 389 U.S. 327, 328 (1967); *Hamilton Shoe Co. v. Wolf Brothers*, 240 U.S. 251, 257-258 (1961); Stern & Gressman, *Supreme Court Practice*, Sec. 4.19 (4th Ed. 1969). A similar rule is followed by the Court with respect to the review of the judgment or decree of the highest court of a state reversing an inferior court and remanding the case for further proceedings.

The decision of the Fifth Circuit is decidedly interlocutory in nature. The Fifth Circuit has only ruled: (i) that Respondent Spector has not made a wholly insubstantial or frivolous claim under SEC Rule 10b-5; and

(ii) that further proceedings are necessary to fully develop the facts of the controversy so as to insure a proper determination of the substantive and jurisdictional issues. In short, the case is not ripe for decision now.

Petitioners simply have not shown that this case is so exceptional, or involves legal questions of such imperative legal importance to the public, as would justify the grant of certiorari at this intermediate juncture of the litigation. The record amply reflects that Respondent has alleged facts substantially similar to those in which the Courts have uniformly held that there is a claim cognizable under Section 10(b) of the Securities Exchange Act and SEC Rule 10b-5. (See pages 8 to 10, *supra*).

In addition, the record reveals that there are material factual controversies between the parties, which among other things involve "close factual questions of intent, reliance, and motive", which bear upon the determination of the substantive and jurisdictional issues. 517 F.2d at 284; Annex A, *infra*. Faced with such fact issues, federal appellate courts have refused to affirm summary judgments previously entered on grounds that no relief was available under Section 10(b) of the Security Exchange Act. *Schoenbaum v. Firstbrook*, 405 F.2d 215, 218 (2nd Cir. 1968) (en banc) cert. denied, 395 U.S. 906 (1969); *Commercial Iron & Metal Co. v. Bache & Co., Inc.*, 478 F.2d 39, 43 (10th Cir. 1973); cf. *Azalea Meats, Inc. v. Muscat*, 386 F.2d 5, 9-10 (5th Cir. 1967).

Surely if fact issues of the type involved herein preclude summary judgment, a dismissal for want of subject matter jurisdiction made at the very commencement of the proceedings and before filing of an answer, cannot be sustained. Since the claim of Respondent Spector as alleged under SEC Rule 10b-5 is not frivolous, he should be given a chance to prove his claim (517 F.2d at 286).

CONCLUSION

For the foregoing reasons, it is respectfully submitted that this petition for a writ of certiorari should be denied.

JOHN KIRK PATTERSON
JAMES D. STEWART

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CERTIFICATE OF SERVICE

I, JOHN KIRK PATTERSON, do certify that copies of the foregoing Respondent's Brief in Opposition have been mailed to: Tinsman & Houser, Inc., 1900 National Bank of Commerce Building, San Antonio, Texas 78205; Cox, Smith, Smith, Hale & Guenther, Inc., 500 National Bank of Commerce Building, San Antonio, Texas 78205; and Davis & O'Conner, 1500 National Bank of Commerce Building, San Antonio, Texas 78205, on this ____ day of December, 1975.

_____

JOHN KIRK PATTERSON

ANNEX A

PARTIAL LIST OF DISPUTED FACTS AND ISSUES

PETITIONERS' CONTENTIONS	RESPONDENT'S CONTENTIONS	REMARKS
1 The purchase by BME of Spector's 18 shares of its stock was not made pursuant to a transaction separate and independent and subsequent to the divorce settlement [App. p. 48.]	1 The purchase by BME of Spector's 18 shares of its stock was made pursuant to a transaction separate and apart and subsequent to the divorce settlement. [App. pp. 271-273, 76; Annex B at p. 16a, infra.]	"Indeed in no less than eight separate documents filed with the Securities and Exchange Commission . . . Defendants repeatedly state and acknowledge that the 18 shares owned by Bernard D. Spector were purchased by BME 'Following the settlement of a divorce proceeding' in March 1972.'" [App. pp. 274-275.]
2 The possibility of BME going public through a syndicate to be managed by E. F. Hutton was well known to Mr. Spector at the time BME purchased his stock. [App. p. 166.]	2 The material facts as to the proposed public offering through E. F. Hutton were willfully concealed from Spector and his attorneys. [Annex B at p. 6a, infra; App. pp. 278, 430-433, 472-473.]	See Stier v. Smith, 473 F.2d 1205, 1208 (5th Cir. 1973) ("Stated in its simplest form, when defendant fails to disclose information, the law will presume that plaintiff would have wanted to know the information if he had an inkling of its existence").
3 BME did not pay Spector the $370,000.00 based upon the value of 18 shares of its stock. [App. p. 49.]	3 BME agreed to pay Spector $370,000.00 for the 18 shares of its stock which he had been awarded in the divorce settlement as his sole and separate property. [Annex B at pp. 16a-19a, infra.]	
4 At the time of BME's purchase of its stock, Spector did not own the 18 shares free and clear. [App. p. 314.]	4 At the time of BME's purchase of its stock, Spector owned the 18 shares free and clear. [App. pp. 272-273; Annex B at pp. 16a, 19a, infra.]	
5 During the divorce settlement negotiations, Spector was never interested in receiving the 18 shares of BME stock as his separate property since the entire thrust of the divorce negotiations was to come to an agreed dollars amount. [App. pp. 168, 49, 313.]	5 During the divorce settlement negotiations, Spector claimed to have community interest in the BME shares and was willing to receive BME stock free and clear as his separate property. [App. pp. 270-271, 43, 53-54.]	See United States v. Diebold, Inc., 369 U.S. 654, 655 (1962) (Even on summary judgment motion, inferences to be drawn must be viewed in the light most favorable to party opposing motion).
6 The Stock Purchase Agreement between BME and Spector was solely a funding arrangement for the divorce, and was not a "real" transaction between BME and Spector. [App. pp. 50, 167.]	6 The Stock Purchase Agreement was a "real" transaction between BME and Spector, and said agreement was reached between Spector's attorneys and the attorneys for BME in reliance upon representations by the latter that there was "no deal" to go public. [Annex B at pp. 6a, 16a-20a; App. pp. 76, 278, 472-473, 430-433.]	See Azalea Meats, Inc. v. Muscat, 386 F.2d 5, 9-10 (5th Cir. 1967); Massey-Ferguson, Inc. v. Bent Equip. Co., 283 F.2d 12, 15 (5th Cir. 1960); Blakely v. American Employers' Insurance Co., 424 F.2d 728, 736 (5th Cir. 1970) (Actions involving fraudulent concealment or the state of mind of a person may not be decided by summary judgment).
7 Spector "never had a stock certificate evidencing such shares which was subject to his unrestricted determination as to whether he would retain or sell the BME shares nor was there any arms-length bargaining with BME . . ." [App. pp. 167-168.]	7 Spector had a stock certificate which he owned free and clear, and for which BME paid to Spector $370,000.00 in a transaction separate and distinct from and subsequent to the divorce. [App. pp. 398-399; Annex B at pp. 16a-21a; Annex F at p. 41a.]	

ANNEX B

PLAINTIFF DEMANDS TRIAL BY JURY

IN THE
UNITED STATES DISTRICT COURT FOR THE
WESTERN DISTRICT OF TEXAS
SAN ANTONIO DIVISION

BERNARD D. SPECTOR,
Plaintiff,
versus CA No. SA-73-CA-285

LQ MOTOR INNS, INC.,
SAMUEL E. BARSHOP, PHILIP M. BARSHOP,
DORIS BARSHOP SPECTOR, and
NORMAN S. DAVIS,
Defendants.

FIRST AMENDED COMPLAINT

Plaintiff, Bernard D. Spector, by his attorneys, Lang, Cross, Ladon, Boldrick & Green, complaining of Defendants, alleges upon information and belief, except as to paragraphs 1 through 4, 11, 12 and 17, which are upon knowledge.

COUNT I

1. The jurisdiction of this Count I is based on § 27 of the Securities Exchange Act of 1934 (the "Exchange Act"), 15 U.S.C. § 78aa, as amended.

2. This Count I is brought under the Exchange Act, and in particular § 10(b), 15 U.S.C. § 78j, and the rules and regulations of the Securities and Exchange Commission promulgated thereunder.

3. The illegal acts complained of herein occurred in substantial part in the Western District of Texas, San Antonio Division.

4. Plaintiff is a citizen of the State of Texas, residing at 6133 Yorkshire, Dallas, Texas.

5. Defendant LQ Motor Inns, Inc. (the "Corporation") is a corporation organized and existing under the laws of the State of Delaware with its principal place of business at the Century Building, 84 N.E. Loop 410, San Antonio, Texas. The Corporation is the successor in interest to the operations of Barshop Motel Enterprises, Inc. ("Enterprises"), which predecessor organization had been founded in 1962 under the laws of the State of Texas. At present the Corporation owns and operates approximately thirty-one (31) motor inns located in Texas, Arizona, New Mexico and Louisiana.

6. Defendant Samuel E. Barshop is a citizen of the State of Texas, residing at 108 Villa Ann, San Antonio, Texas. He is President and Director of the Corporation; and presently owns approximately 22.8% of its outstanding common stock. He held similar positions with Enterprises since its inception.

7. Defendant Philip M. Barshop is a citizen of the State of Texas, residing at 105 Lou Jon, San Antonio,

Texas. He is Executive Vice President, Secretary and Director of the Corporation; and presently owns approximately 22.4% of its outstanding common stock. He was a Vice President and a Director of Enterprises since its inception.

8. Defendant Doris Barshop Spector is a citizen of the State of Texas, residing at 107 Cas-Hills, San Antonio, Texas, and is the sister of Defendants Samuel E. Barshop and Philip M. Barshop. She presently owns approximately 12.7% of the outstanding capital stock of the Corporation. She was a Director and Shareholder of Enterprises.

9. Defendant Norman S. Davis is a citizen of the State of Texas, residing at 215 Paseo Encinal, San Antonio, Texas. Mr. Davis directly and indirectly owns approximately 38,753 shares of the common stock of the Corporation. From the Corporation's inception in June, 1972 until approximately July, 1973, Mr. Davis was Secretary, General Counsel, and Director of the Corporation. He was a Secretary of Enterprises and Counsel since its inception. As is also the case of the other individual Defendants, Mr. Davis at all relevant times was a "controlling person" within the meaning of Section 20 of the Exchange Act, 15 U.S.C. § 78t.

10. Beginning approximately June, 1971 and until March 16, 1972, individual Defendants Samuel E. Barshop, Philip M. Barshop and Norman S. Davis, acting singly and in concert, had discussions and made plans as to the public sale of the securities of Enterprises and/or possible methods of public financing for Enterprises. In particular, representatives of Defen-

dants and E. F. Hutton & Company, Inc. had discussions, made plans, and took steps to effectuate an exchange offer wherein and whereby a new corporation would be formed to acquire from Enterprises all of its assets and business. Upon the consummation of the said exchange offer, there would be a public offering through E. F. Hutton & Company, Inc. of the shares of the new corporation, which public offering would also include the sale of certain shares owned by Defendants Samuel E. Barshop, Philip M. Barshop, and Doris Barshop Spector.

11. On several occasions between December, 1971 and March 16, 1972, Defendants, by their representative and attorney, Norman S. Davis, stated to Plaintiff and his attorneys that Enterprises desired to enter into a transaction whereby it would acquire from Plaintiff his eighteen (18) shares of common stock of Enterprises, said eighteen (18) shares being approximately 15% of the total then outstanding shares of Enterprises. Upon receipt of this information, Plaintiff and his attorneys on at least one occasion inquired as to the current status of any efforts by Enterprises to effectuate a public sale of its securities. In response to that inquiry, Defendants caused their agents to represent that, ". . . there is not presently in effect any contractual agreement for any such public financing, sale of securities, or merger."

12. In reliance upon the aforesaid representations and the integrity of the individual Defendants, Plaintiff on March 16, 1972, entered into a written Agreement For Purchase of BME Stock, a copy of which is made a part hereof and which is attached hereto as Exhibit "A".

13. With regard to the written agreement and transaction described in paragraph 12 wherein Plaintiff sold to Enterprises his eighteen (18) shares of its common stock, the Defendants willfully concealed from Plaintiff the material facts as to the proposed "public offering" by a syndicate to be managed by E. F. Hutton & Company, Inc. Had Defendants made such disclosures, Plaintiff would have refused to sell his common stock, or any part thereof, at the price at which it was actually sold.

14. The fraud practiced and the devise utilized by the Defendants consisted *inter alia* of the representation that:

> ". . . [T]here have been discussions with various brokerage houses in the past concerning such public sale of securities and for public financing . . . and that such discussions are continuing and are expected to continue in the future, but BME ("Enterprises") has warranted to Spector that there is not presently in effect any contractual agreement for any such public financing . . ." (Reference added)

This representation was materially false and misleading in that it omitted to state the material facts as to the proposes exchange offer and public financing through E. F. Hutton & Company, Inc. Accordingly, the Defendants failed to state material facts necessary in order to make the statements made in light of circumstances not misleading.

15. Shortly after the transaction set forth in paragraphs 12 and 13, Defendants Samuel E. Barshop,

Philip M. Barshop and Doris Barshop Spector acquired from Enterprises the said eighteen (18) shares for an aggregate of $370,000.00 which sum was paid in substantial part by their assumption of a promissory note.

16. As a part of and in furtherance of the plan which operated as a fraud and deceit upon Plaintiff, Defendants beginning approximately May, 1972 acting singly and in concert, caused the necessary papers to be prepared and filed to form the Corporation. In June, 1972, the corporate charter was granted pursuant to the laws of the State of Delaware as to the Corporation. Thereafter the Corporation acting by and through its directors, officers, and the individual Defendants as stockholders aided and abetted and participated in concert with the other Defendants in activities in furtherance of the fraudulent plan, which is more fully described above.

17. On June 29, 1972, Defendants caused a Form S-1 Registration Statement (Registration No. 2-44883) to be filed under the Securities Act of 1933, 15 U.S.C. § 77a *et seq*. Said registration statement being filed as to the public sale, by means of an exchange offer, of not less than 250,000 shares of common stock of the Corporation, at an initial public offering price of not less than $13.25 per share.

18. On March 21, 1973, the public sale of 280,000 shares of common stock of the Corporation was effectuated by a syndicate of financial underwriters represented by E. F. Hutton & Company, Inc. As selling stockholders in the public offering, individual Defendants Samuel E. Barshop, Philip M. Barshop and

Doris Barshop Spector sold in excess of 157,243 shares of common stock of the Corporation, realizing therefrom proceeds of $12.30 per share. Of the shares sold by said, individual Defendants, 151,406 shares had been acquired by them in exchange for the eighteen (18) shares of Enterprises' common stock which had been received from Plaintiff on March 16, 1972. Said individual Defendants, therefore, realized total proceeds of $1,862,294.00 for the securities which had been acquired from Plaintiff at a cost of $370,000.00 (i.e., cost of $2.44 per share). The Corporation at said public offering sold 50,000 of its shares, realizing proceeds therefrom of $615,000.00.

19. Defendants acted singly and in concert, aiding and abetting each other, in connection with the representations and matters complained of; and directly and indirectly utilized the mails and other instrumentalities in interstate commerce. Defendants' willful concealment of the aforesaid material inside information has caused Plaintiff to suffer damages in excess of $1,144,406.00.

WHEREFORE, Plaintiff demands judgment:

A. For rescission of the sale by Plaintiff to Enterprises for the sum of $370,000.00 (which amount Plaintiff hereby agrees to return to Defendants) of Plaintiff's eighteen (18) shares of Enterprises, and conversion of same into 151,406 shares of common stock of the Corporation, par value $.10 per share; and/or

B. Against Defendants, jointly and severally, for the damages suffered by Plaintiff as the result of

Defendants' aforesaid wrongful conduct, which damages exceed $1,144,406.00, plus interest; and

C. Costs and expenses of this action, including reasonable attorneys' and accounting fees; and

D. Such other and further relief as may be necessary and appropriate.

COUNT II

20. Paragraphs 3 through 19 of Count I are incorporated into this Count II by reference.

21. Jurisdiction of this Count II is based upon the principles of pendent jurisdiction.

22. This Count II is brought to enforce the liability imposed upon Defendants by Section 33 of the Texas Security Act, Vernon's Ann. Civ. St. Art. 581-33.

WHEREFORE, Plaintiff demands judgment:

A. Against Defendants, jointly and severally, for the actual damages sustained by Plaintiff as the result of Defendants' wrongful conduct, which damages exceed $1,144,406.00, plus interest; and

B. Against Defendants, jointly and severally, for punitive or exemplary damages in an amount of twice the actual damages suffered; and

C. Costs and expenses of this action, including reasonable attorneys' and accounting fees; and

D. Such other and further relief as may be necessary and appropriate.

COUNT III

23. Paragraphs 3 through 19 of Count I are incorporated into this Count III by reference.

24. Jurisdiction of this Count III is based upon principles of pendent jurisdiction.

25. The individual Defendants as representatives of all the shareholders and the managing directors of Enterprises owed fiduciary duties to each shareholder of Enterprises to deal with him fairly and impartially, and not for the sole benefit of the majority shareholders to the prejudice and detriment of a minority shareholder, such as the Plaintiff.

26. Plaintiff, on and before March 16, 1972, had no knowledge of the discussions, plans, and steps taken with representatives of E. F. Hutton & Company, Inc. as to the proposed exchange offer and public sale of Enterprises' securities. If Plaintiff had possessed knowledge of said decisions, plans, and steps taken, he would have refused to sell his stock at the price it was sold.

27. The purchase of Plaintiff's stock under the circumstances constituted the oppressive operation of corporate machinery for the sole benefit of the other shareholders to the prejudice and the detriment of the Plaintiff. Such purchase constituted a breach of the aforesaid fiduciary duties that Enterprises and the individual Defendants owed to Plaintiff.

28. On account of such breaches of duty, Plaintiff is entitled to have Defendants deliver to him 151,406 shares of common stock of the Corporation, par value $.10 per share. In the alternative, Plaintiff is entitled to his damages against Defendants, jointly and severally, in an amount in excess of $1,144,406.00.

WHEREFORE, Plaintiff demands judgment:

A. For rescission of the sale by Plaintiff to Enterprises for the sum of $370,000.00 (which amount Plaintiff hereby agrees to return to Defendants) of Plaintiff's eighteen (18) shares of Enterprises, and conversion of same in to 15,406 shares of common stock of the Corporation, par value $.10 per share; and/or

B. Against Defendants, jointly and severally, for the actual damages suffered by Plaintiff as the result of Defendants' wrongful conduct, which damages exceed $1,144,406.00, plus interest; and

C. Costs and expenses of this action, including reasonable attorneys' and accounting fees; and

D. Such other and further relief as may be necessary and appropriate.

COUNT IV

29. Paragraphs 3 through 19 of Count I, and paragraph 25 through 27 of Count III are incorporated into this Count by reference.

30. Jurisdiction of this Count IV is based upon the principles of pendent jurisdiction.

31. The representations of Defendants heretofore described under common law principles constituted a fraud committed upon Plaintiff and a fraud in the inducement of contract.

WHEREFORE, Plaintiff demands judgment:

A. For rescission of the sale by Plaintiff to Enterprises for the sum of $370,000.00 (which amount Plaintiff hereby agrees to return to Defendants) of Plaintiff's eighteen (18) shares of Enterprises, and conversion of same into 151,406 shares of common stock of the Corporation, par value $.10 per share; and/or

B. Against Defendants, jointly and severally, for the actual damages suffered by Plaintiff as the result of Defendants' wrongful conduct, which damages exceed $1,144,406.00, plus interest; and

C. Costs and expenses of this action, including reasonable attorneys' and accounting fees; and

D. Such other and further relief as may be necessary and appropriate.

COUNT V

32. Paragraphs 3 through 19 of Count I, and paragraphs 25 through 27 of Count III, are incorporated into this Count V by reference.

33. Jurisdiction of this Count V is based upon the principles of pendent jurisdiction.

34. The aforesaid acts of Defendants Samuel E. Barshop, Philip M. Barshop and Doris Barshop Spector whereby they caused Enterprises to purchase Plaintiff's shares for the purpose of appropriating to themselves the fair market value of Plaintiff's shares in excess of $370,000.00 constitute an unjust enrichment at Plaintiff's expense.

35. The amount of the excess of fair market value of Plaintiff's stock in Enterprises over $370,000.00 exceeds $1,144,406.00.

36. On account of such unjust enrichment, Plaintiff is entitled to have Defendants deliver to him 151,406 shares of common stock of the Corporation, $.10 par value. Plaintiff stands ready to refund to Defendants the purchase price of his stock. In the alternative, Plaintiff is entitled to damages against Defendants, jointly and severally, in excess of $1,144,406.00.

WHEREFORE, Plaintiff demands judgment:

A. For rescission of the sale by Plaintiff to Enterprises for the sum of $370,000.00 (which amount Plaintiff hereby agrees to return to Defendants) of Plaintiff's eighteen (18) shares of Enterprises, and conversion of same into 151,406 shares of common stock of the Corporation, par value $.10 per share; and/or

B. Against Defendants, jointly and severally, for the damages suffered by Plaintiff as the result of Defendants' wrongful conduct, which damages exceed $1,144,406.00, plus interest; and

C. Costs and expenses of this action, including reasonable attorneys' and accounting fees; and

D. Such other and further relief as may be necessary and appropriate.

San Antonio, Texas
January 24, 1974.

LANG, CROSS, LADON,
BOLDRICK & GREEN

/s/ ERNEST J. ALTGELT, III
Attorney in Charge
1540 Milam Building
San Antonio, Texas 78205
Tel: (512) 227-3106
ATTORNEYS FOR PLAINTIFF

OF COUNSEL:

ERNEST J. ALTGELT III

DEMAND FOR JURY TRIAL

A jury trial is demanded on all counts of this complaint.

/s/ ERNEST J. ALTGELT, III
ERNEST J. ALTGELT III

VERIFICATION

THE STATE OF TEXAS
COUNTY OF BEXAR

BERNARD D. SPECTOR, being duly sworn, deposes and says: that he is a plaintiff in the within action; that he has read the foregoing First Amended Complaint and knows the contents thereof; that the same is true to his own knowledge, except as to the matters therein stated to be alleged on information and belief, and that as to those matters, he believes it to be true.

/s/ BERNARD D. SPECTOR
Bernard D. Spector

SUBSCRIBED and SWORN TO before me this 24th day of January, 1974.

/s/ TOM COGHLAN
Notary Public in and for
Bexar County, Texas

First Amended Complaint

EXHIBIT "A"

AGREEMENT FOR PURCHASE OF BME STOCK

This Agreement made and entered into this the 16th day of March, 1972, by and between BERNARD D. SPECTOR (hereinafter sometimes called "Spector") and BARSHOP MOTEL ENTERPRISES, INC., a Texas corporation (hereinafter sometimes called "BME").

RECITALS

1. Spector and his wife, Doris B. Spector, have entered into a Property Settlement Agreement which has been approved by the Court and incorporated in a Divorce Decree this day entered in Cause No. F-218-805 in the 166th Judicial District Court of Bexar County, Texas, said cause being styled Doris B. Spector v. Bernard D. Spector; and under the terms of said Property Settlement Agreement and Divorce Decree Spector owns, free from any claims by Doris B. Spector, eighteen (18) shares of the Common Stock of BME (said eighteen shares BME stock hereinafter sometimes being referred to as "Spector Stock").

2. Spector has made such investigations of the financial affairs and business operations of BME and its subsidiaries as Spector considered necessary and appropriate in his independent judgment for Spector to make a determination of the present fair value of said Spector Stock. In this connection, Spector acknowledges that he is familiar with the operations of BME, its subsidiaries, and all of its assets and operations; that he assisted in the formation of the

motel operations which have come to be known as BME and participated from the inception of operations of the predecessor of BME, being Rodeway-San Antonio-Main Avenue, Inc. (hereinafter sometimes called "Main Avenue"), to October, 1969, in its tax planning and the planning of its operations; that Spector and his agents have been furnished full access to all of the books and records of BME, including all of its subsidiaries and all of the joint ventures and operations involving BME; that he has been informed of the following facts: BME has entered into and plans to enter into numerous joint ventures with individuals, partnerships, corporations and other entities for the construction and/or operation of motels and/or other real estate properties; BME is engaged in negotiating and plans to negotiate additional joint ventures with individuals, partnerships, corporations and other entities for the construction and/or operation of motels and/or other real estate properties; BME has negotiated a Joint Venture Agreement with Prudential Insurance Company and its affiliate, PIC Realty Company, for the construction, financing, and operation of motor hotels; BME has contemplated and considered, and is now contemplating and considering the possibility of substantial expansion, including the possibility of mergers into or with third parties, and possible acquisitions of other real estate and motel interests; BME and/or its principal stockholders have considered and discussed and are considering and discussing possible public sale of securities of BME and/or possible methods of public financing for BME and/or portions of its operations, and in this connection Spector has been advised that there have been discussions with various brokerage

houses in the past concerning such public sale of securities and/or public financing and/or mergers with third parties and that such discussions are continuing and are expected to continue in the future, but BME has warranted to Spector that there is not presently in effect any contractual agreement for any such public financing, sale of securities, or merger. Spector has taken into careful consideration each and all of such elements, as well as the future possibilities for expansion and improvements of BME's earnings and/or possible increase in the value of BME corporate stock, in arriving at his decision to sell said Spector Stock to BME at the price set out herein.

3. Spector has determined to his complete satisfaction that the sum of $370,000 would be a fair and reasonable price for the purchase of all of the Spector Stock from him, and Spector has offered to sell all of said Spector Stock to BME for the said $370,000 price.

AGREEMENT

NOW, THEREFORE, for and in consideration of the premises and the mutual covenants and provisions contained herein and other good and valuable consideration paid to Spector, receipt of which is hereby acknowledged, Spector and BME agree as follows:

1. *Definitions.*

1.1. *Closing.* This instrument is being executed and delivered by the parties, and the closing of the transaction herein contemplated is being closed by the parties, subsequent to the entry of the Divorce Decree in

the above mentioned Cause No. F-218,805 in the 166th Judicial District of Bexar County, Texas.

1.2. *Spector Stock*. The term "Spector Stock" refers to the eighteen (18) shares of corporate stock of BME owned by Spector and represented by Stock Certificate No. 5 of BME, a copy of which is attached hereto as Exhibit A.

2. *Sale of Stock*

Spector hereby agrees to sell to BME and BME hereby agrees to purchase from Spector eighteen (18) shares of the Common Stock of BME (said Spector Stock), being all of the Common Stock owned or claimed by Spector in BME or its subsidiaries, said stock being evidenced by said Stock Certificate No. 5 of BME.

3. *Purchase Price.*

The total consideration to be paid by BME to Spector for said Spector Stock shall be $370,000 to be paid as follows:

3.1. $70,000 shall be paid in cash by BME to Spector at the Closing of this Agreement, at which time Spector shall endorse and deliver to BME said Stock Certificate No. 5 of BME, representing all interest Spector has or claims in BME.

3.2. The remaining $300,000 shall be represented by a Promissory Note from BME payable to the order of Spector (said note to be

in the form attached hereto as Exhibit B) and delivered to Spector at the Closing. Such note will be a negotiable instrument and shall be executed by a duly authorized officer of BME. Payment of such BME Note shall be personally guaranteed by Samuel E. Barshop and Philip M. Barshop.

3.3. The Promissory Note described in Paragraph 3.2. above shall be collateralized by a pledge of said Spector Stock in the form of Collateral Pledge attached hereto as Exhibit C, which Collateral Pledge shall be duly executed and delivered by BME to Spector, at the Closing of this Agreement.

3.4 At the Closing, BME shall give Spector such evidence of corporate authority as may be required by Spector's attorneys to show (a) that the execution of said note and Collateral Pledge have been duly authorized by the directors of BME and is not prohibited by the Articles of Incorporation or By-Laws of BME, (b) that BME has retained earnings in excess of $370,000 at the time of the execution of this agreement, and (c) that upon delivery of said note to Spector the same will constitute a valid legal obligation of BME, collectible from BME in accordance with its terms.

EXECUTED IN DUPLICATE ORIGINALS the day and year first above written.

BARSHOP MOTEL
ENTERPRISES, INC.

/s/ SAMUEL E. BARSHOP
PRESIDENT

/s/ BERNARD D. SPECTOR
BERNARD D. SPECTOR

at 2:15 p.m. 3/16/72
Signing witnessed
/s/ NILES CHUBB
Vice-President
and Senior Trust Officer

APPROVED AS TO FORM:
/s/ NORMAN DAVIS
Attorney for Barshop
Motel Enterprises, Inc.

/s/ JAMES D. STEWART
Attorney for Bernard D. Spector

ANNEX C

Excerpts from Property Settlement Agreement

PROPERTY SETTLEMENT, SUPPORT, AND MAINTENANCE AGREEMENT

DORIS B. SPECTOR

versus

BERNARD D. SPECTOR

Filed: March 16, 1972

This Agreement made and entered into this the 16th day of March, 1972, by and between DORIS B. SPECTOR (the Wife) and BERNARD D. SPECTOR (the Husband), hereinafter sometimes collectively referred to as "the Parties,"

WITNESSETH:

WHEREAS, the Parties are Husband and Wife, having been married on or about the 26th day of December, 1953, in San Antonio, Bexar County, Texas; and,

WHEREAS, diverse disputes and unhappy differences have arisen between the Wife and the Husband, for which reasons they have separated and are now living separate and apart from each other and the Wife has instituted suit for divorce in the 166th Judicial District Court of Bexar County, Texas, same being styled *Doris B. Spector v. Bernard D. Spector*, and bearing Cause No. F-218, 805, said cause having

been filed on or about the 18th day of December, 1969; and wherein Husband filed an Answer and Cross Action; and,

WHEREAS, each of the Parties acknowledges and affirmatively represents that this Agreement has been reached after certain financial books and records of the various partnerships, corporations, and other entities in which Bernard D. Spector and/or Doris B. Spector have a Property Interest (as hereinafter defined) were made available (i) by Bernard D. Spector and his agents to Doris B. Spector and her agents, and (ii) by Doris B. Spector and her agents to Bernard D. Spector and his agents, for inspection by each of the Parties and their respective attorneys and accountants, and that each Party has personally made or had his or her attorneys and Certified Public Accountants in his or her employ make such investigations and analyses as he, she, or they desired of the books and records relating to the Property Interests appearing on or referred to in:

(1) the attached Exhibits A and/or D, and/or

(2) the Federal Income Tax Returns for the calendar years 1953 through 1970 of Doris B. Spector and/or Bernard D. Spector, and/or

(3) the Federal Income Tax Returns and/or Partnership Returns (Form 1065) of the business entities (corporate, partnerships, or joint ventures) relating to the Property Interests listed on the at-

tached Exhibits A and/or D, filed for each fiscal year during the period January 1, 1967 through December 31, 1970, and/or

(4) the checkbook of the Frost National Bank checking account known to the Parties as "the Doris Barshop Spector Real Estate Account," and/or

(5) "Schedule of Transactions" of Doris Barshop Spector Real Estate Account" heretofore furnished to Bernard D. Spector and his accountants, a copy of which "Schedule of Transactions" is attached hereto as Exhibit E; in this regard, Bernard D. Spector shall be bound by the transcribing of the transactions as reflected by the checks and check stubs (whether on front or back thereof), but not by any conclusions drawn therefrom by the accountant in his preparation of such Schedule;

and each Party further acknowledges that neither Party nor his or her attorneys nor any of his or her agents have refused at any time that this divorce proceeding has been pending to make available to the other Party or his or her attorneys or accountants any information, books, or records which they have requested pertaining to the financial affairs of either Party since 1953, the year in which the Parties were married; and,

* * *

Excerpts from Property Settlement Agreement

NOW, THEREFORE, FOR AND IN CONSIDERATION OF THE PREMISES and the mutual covenants and provisions herein contained and other good and valuable consideration, receipt of which is hereby acknowledged, Husband and Wife agree as follows:

1. *DISPOSITION OF COMMUNITY PROPERTY.*

1.1. The community assets and liabilities existing as of the date hereof, which were acummulated during the marriage of the Parties, consist of those Property Interests listed on Exhibit A, attached hereto, and including but not limited to those liabilities listed on Exhibit A attached hereto. The Parties hereby agree to this property settlement agreement wherein the separate property (and liabilities related thereto) of each of the Parties is to be set aside to such Party and the community property and liabilities are to be divided as herein set out, such division of the community property being an equal division between them with respect to the total value of all Community Property interests involved and such division being fair, just, and equitable.

1.2. Bernard D. Spector shall own without any claim on the part of Doris B. Spector, all community assets listed on Exhibit B, attached hereto and Bernard D. Spector shall assume and pay all community liabilities specifically listed on Exhibit B, attached hereto, and agrees to hold Doris B. Spector free and harmless of any liability therefrom.

1.3. Doris B. Spector shall own, without any claim on the part of Bernard D. Spector, all community

assets listed on Exhibit C, attached hereto, subject to any and all indebtedness thereon; and Doris B. Spector shall assume and pay all liabilities listed on Exhibit C, attached hereto, and all community liabilities not specifically assumed herein by Bernard D. Spector and agrees to hold Bernard D. Spector free and harmless of any liability therefrom.

* * *

21. *BINDING EFFECT.*

This Agreement shall be binding upon the heirs, legal representatives, and assigns of both Parties hereto.

IN WITNESS WHEREOF, the Parties have signed and acknowledged this Agreement.

/s/ DORIS B. SPECTOR
DORIS B. SPECTOR
/s/ BERNARD D. SPECTOR
BERNARD D. SPECTOR

APPROVED AS TO FORM:
/s/ A. R. SOHN
ATTORNEY FOR DORIS B. SPECTOR
/s/ JAMES D. STEWART
ATTORNEY FOR BERNARD D. SPECTOR

STATE OF TEXAS
COUNTY OF BEXAR

BEFORE ME, the undersigned authority, on this day personally appeared DORIS B. SPECTOR, known to

me to be the person whose name is subscribed to the foregoing instrument, and acknowledged to me that she executed the same for the purposes and consideration therein expressed.

GIVEN UNDER my hand and seal of office this 16th day of March, 1972.

/s/ J. RUSSELL DERG
NOTARY PUBLIC,
BEXAR COUNTY, TEXAS

STATE OF TEXAS
COUNTY OF BEXAR

BEFORE ME, the undersigned authority, on this day personally appeared BERNARD D. SPECTOR, known to me to be the person whose name is subscribed to the foregoing instrument, and acknowledged to me that he executed the same for the purposes and consideration therein expressed.

GIVEN UNDER my hand and seal of office this 16th day of March, 1972.

/s/ J. RUSSELL DERG
NOTARY PUBLIC,
BEXAR COUNTY, TEXAS

Excerpts from Property Settlement Agreement

EXHIBIT A

PROPERTY SETTLEMENT, SUPPORT AND MAINTENANCE AGREEMENT

COMMUNITY ASSETS AND LIABILITIES

ASSETS

All property interests owned by BERNARD D. SPECTOR and/or DORIS B. SPECTOR, which the parties knew of or should have known, in and to each of the following:

1. Atlantic Richfield Corporation.

2. Barshop Motel Enterprises, Inc., a Texas corporation, and all of its affiliate and subsidiary operations.

* * *

EXHIBIT B

PROPERTY SETTLEMENT, SUPPORT, AND MAINTENANCE AGREEMENT

COMMUNITY ASSETS TO BE RECEIVED BY BERNARD D. SPECTOR

1. Eighteen (18) shares of corporate stock of Barshop Motel Enterprises, Inc., a Texas corporation.

2. Note receivable from Bielstein, Lewis & Wilson with an unpaid balance of approximately $47,000.

* * *

Excerpts from Property Settlement Agreement

EXHIBIT C

PROPERTY SETTLEMENT, SUPPORT AND MAINTENANCE AGREEMENT

COMMUNITY ASSETS TO BE RECEIVED BY DORIS B. SPECTOR

1. Twenty-two (22) shares of corporate stock of Barshop Motel Enterprises, Inc., a Texas corporation.

2. Eight percent (8%) undivided interest in Empire Plaza Shopping Center, a partnership (Federal Employer Identification No. 74-1665900).

3. One Hundred and Fifty-One (151) shares of corporate stock in San Antonio Produce Terminal Market, a Texas corporation.

4. All rights, title and interest in and to the home property occupied by Doris B. Spector located at 107 Cas-Hills, in the city of San Antonio, Bexar County, Texas, and all furniture, fixtures, and other personal property located therein.

* * *

EXHIBIT D

PROPERTY SETTLEMENT, SUPPORT AND MAINTENANCE AGREEMENT

SEPARATE PROPERTY OF DORIS B. SPECTOR

Excerpts from Property Settlement Agreement

All Property Interests which the parties knew of or should have known, in and to each of the following:

1. Alamo Downs (Federal Employer Identification No. 74-6066023), a partnership which owns, among other interests, approximately 338 acres at the corner of Culebra Road and Loop 410 in San Antonio, Texas.

2. Austin Highway Enterprises, Inc., a Texas corporation.

* * *

ANNEX D

Judgment of Divorce

IN THE DISTRICT COURT
166th JUDICIAL DISTRICT
BEXAR COUNTY, TEXAS

DORIS B. SPECTOR

versus NO. F-218, 805

BERNARD D. SPECTOR

JUDGMENT

On this the 16th day of March, 1972, came on to be regularly heard the above styled and numbered cause, after the same was regularly set and called for trial, and came the Plaintiff in person and by and through her attorneys-of-record, and came the Defendant in

person and by and through his attorneys-of-record, and both parties announced ready for trial, and it appearing to the Court from an inspection of the record and from the evidence that Plaintiff's Petition has been on file in this Court for more than sixty full days and that Plaintiff is and has been an actual bona fide inhabitant of the State of Texas for a period of more than twelve months next preceding the filing of Plaintiff's Petition herein, and also has resided in Bexar County, Texas, for more than six months next preceding the filing of this suit; and the Defendant having moved in open Court that he desires to take a Non-Suit on his Cross-Action herein, which motion for Non-Suit was granted; and a jury having been waived by each of the parties hereto, the Court proceeded to try said cause, and thereupon all matters in controversy as well of fact and of law were submitted to the Court, and the Court having heard the pleadings read and the evidence and argument of counsel is of the opinion that the material facts alleged in Plaintiff's Petition have been fully proven by full and satisfactory evidence and that she is entitled to a divorce from the Defendant.

IT IS, THEREFORE, ORDERED, ADJUDGED and DECREED by the Court that the bonds of matrimony heretofore and now existing between the Plaintiff, DORIS B. SPECTOR, and the Defendant, BERNARD D. SPECTOR, be, and the same are hereby, dissolved, and the Plaintiff is hereby divorced from the Defendant.

And it further appearing to the Court that the Plaintiff and Defendant had born to them during their marriage four (4) children, to-wit: JOCELYN MARIE

SPECTOR, born August 6, 1955; JACK JOSHUA SPECTOR, born May 25, 1957; MITCHEL BARSHOP SPECTOR, born January 11, 1959; and LISA GAIL SPECTOR, born July 27, 1965, all being under the age of eighteen years; and the Court having found from the evidence that it would be to the best interests of such children that their care, custody and control be awarded to Doris B. Spector, the Plaintiff herein, with the right of Bernard D. Spector, the Defendant herein, to be and visit with such children at all reasonable times and at all reasonable places, upon first giving reasonable notice to the Plaintiff of his intention to do so; and the Court finds from the evidence that the Defendant should contribute to the Plaintiff One Hundred and Seventy-Five Dollars ($175.00) per month per child for the support and maintenance of each such child until each such child reaches his or her eighteenth birthday; that such payments are to be made directly to the Plaintiff on the first day of each month, commencing on the first day of April, 1972, and continuing on the first day of each month thereafter until each child reaches the age of eighteen years.

IT IS, THEREFORE, ORDERED, ADJUDGED and DECREED that the care, custody, and control of the four minor children above set out be and are hereby awarded to the Plaintiff, DORIS B. SPECTOR, with the right of the Defendant, BERNARD D. SPECTOR, to be and visit with such children at all reasonable times and at all reasonable places, after first giving reasonable notice of his intention to do so to the Plaintiff.

IT IS FURTHER ORDERED, ADJUDGED, and DECREED that the Defendant, BERNARD D. SPECTOR,

pay to the Plaintiff, DORIS B. SPECTOR, the sum of One Hundred and Seventy-Five Dollars ($175.00) per month per child for the support and maintenance of each of the said four children, until each such child reaches his or her eighteenth birthday, the first such payment to commence on the first day of April, 1972, and to continue on the first day of each month thereafter until each child reaches the age of eighteen years.

And it appearing to the Court that the Plaintiff and Defendant have made a settlement of their community and separate property rights in a Property Settlement Agreement entered into by the Plaintiff and the Defendant, and the Court, after having examined said Property Settlement Agreement and heard evidence thereon, finds the same to be fair, just and equitable to both the Plaintiff and the Defendant.

IT IS, THEREFORE, ORDERED, ADJUDGED, and DECREED by the Court that said Property Settlement Agreement entered into by and between the Plaintiff and the Defendant be, and the same is hereby, approved by the Court and ordered filed among the papers in this cause, and the same is made a part of this Decree as though copied herein in full, and it is further ORDERED that Plaintiff shall be permitted to withdraw said Property Settlement Agreement from the papers in this cause after the same has been so filed by signing a receipt therefor.

IT IS FURTHER ORDERED, ADJUDGED and DECREED by the Court that each of the parties shall execute and deliver to the other, on demand, such docu-

ment or documents or other instruments, as may be reasonably necessary or proper to effectuate the vesting of the title to the properties in accordance with the terms of such Property Settlement Agreement and this judgment.

IT IS FURTHER ORDERED, ADJUDGED, and DECREED by the Court that all other relief prayed for by either of the parties be, and the same is hereby, denied.

IT IS FURTHER ORDERED, ADJUDGED and DECREED by the Court that all costs of this suit herein incurred are judged to be paid one-half (½) by the Plaintiff and one-half (½) by the Defendant, for which sums let execution and such other writs as may be necessary issued: PROVIDED, HOWEVER, the Plaintiff and the Defendant shall each pay all charges relating to depositions taken by such party in conjunction with this lawsuit.

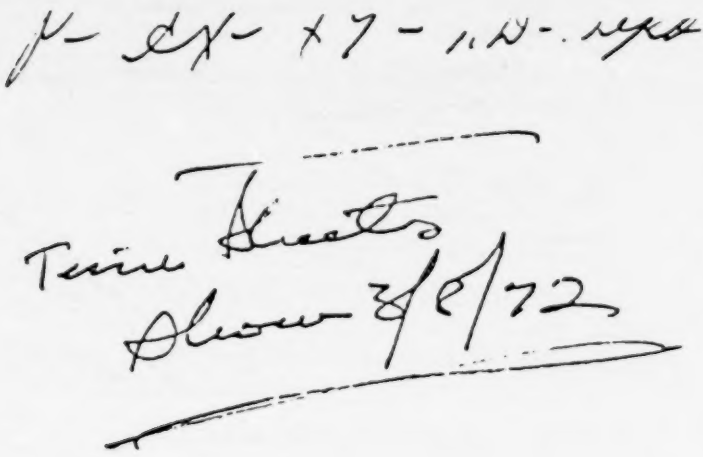
SIGNED this 16th day of March, 1972 at 1:30 P.M. APPROVED:

/s/ ROBERT R. MURRAY
JUDGE PRESIDING

/s/ A. R. SOHN
Attorney for Plaintiff
/s/ JAMES D. STEWART
Attorney for Defendant
/s/ DORIS B. SPECTOR
/s/ BERNARD D. SPECTOR
Bernard D. Spector

ANNEX E

Handwritten Notes taken by petitioner Norman S. Davis at meeting with representatives of E. F. Hutton & Company on March 8, 1972, one week before B.M.E.'s purchase of Respondent's stock (showing solid plans for going public)



3/15/72 - COME WITH 25 OF EACH ITEM

JOHN STANTON -
CHRIS ROTE -
MARK SHAPIRO -

ASSUME =
5/31 = Closing Year
8/15 = Financials Completed + File/SEC

OUT IN OCTOBER

HIT HIT HIT HIT HIT HIT HIT HIT

PROBLEMS =

1. OFFERING TO PARTNERS =
   Need prospectus to partners?
   Do we need separate "stages"?
   → How was Eulich/Rodeway handled?
   Participation by partners in expenses

2. PACKAGE TO BE OFFERED =
   Ps suggests min. play. of about 300,000 shares/Common at around $15 = total play. of $4.5 to $5 mm.
   Will [illegible] determine what funds the Corp. needs + add to that the (2) Any deals any partners want

to sell + (3) or so Sam/Phil/Doris can join us selling stuff if they want some cash.

[Sam: Enoch will probably want to sell all of his stock in the Initial Offering] =

→ Want to be sure we don't get too distracted by all of our partners holding so much stock they resume.

3. What Partner is a Cop = Does BMC get the cooperation of the Partners wants

4. Q: "Can [HUTTON] provide some kind of [the Partners] own valuation of the entire Co. as a "quasi-liquidity event" = then use that to price the subscription of services = paid value of Partners' "illiquidity" [franchise, etc.]

→ WARP: the "division" to be based on PRIVATE-TYPE valuations [e.g. 8 times Cash Flow as of Last Qtr]

5. SIMULTANEOUS CLOSING —
Plan to have partners "committed" in advance —

multiple on [low range of Public] depending on ratio of a minimum of ____ to ____ not less than 80% - 90% of X times earnings

6. FINANCIALS = PRO FORMAS NEEDED for 5 yrs. ended 5/31/72

7. Need to start on "Evaluations of Syndication w. Partners"

8. DRAFTING OF PROSPECTUS:

(1) NSD / JHP / HARRY to start
(2) Hilton to take crude indication info
(3) Dev. to add Mechanical Section

"MANAGER'S FEE" →

Assuming "8% selling discount" - Management [C.F. Hutton] would get 20% of total discount as Management =

In this case = 8% / 1.5 mil = 380,000 + 20% = 76,000 manager's fee

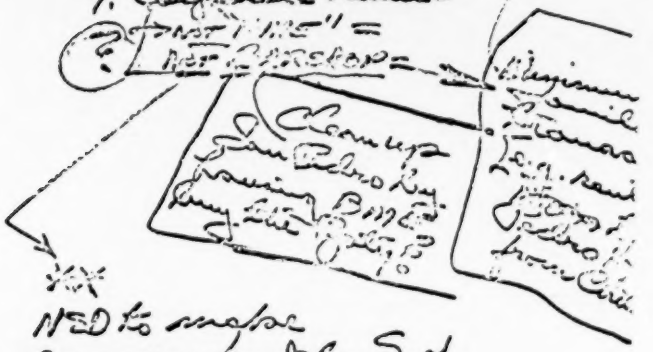
MARK to send us cc/5-6 late Model PROSPECTUSES =

9- PRICING =

IS = We Buy "Price" slightly below comparable seasoned public Companies =

10- FOR BEST IMAGE =

1. Good earnings =
2. Clean Transactions =
3. "Good" BOARD DIRECTORS -
4. Corporate name =



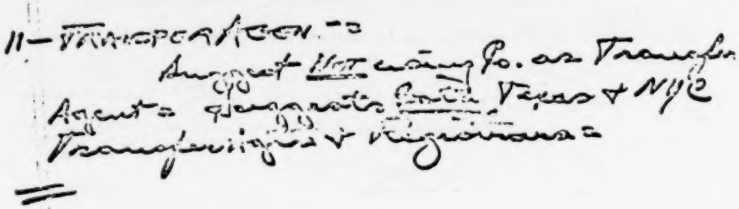
NED to make summary for John S. of "Enchanted Rock"

- HOUSTON TOWERS
- CORPUS MARINA =
- NEW LA-QUINTA =
- HOU. INTERNATIONAL AIRPORT

NED Note: Clean up + amend Rep. Charter before going Public

Handwritten Notes

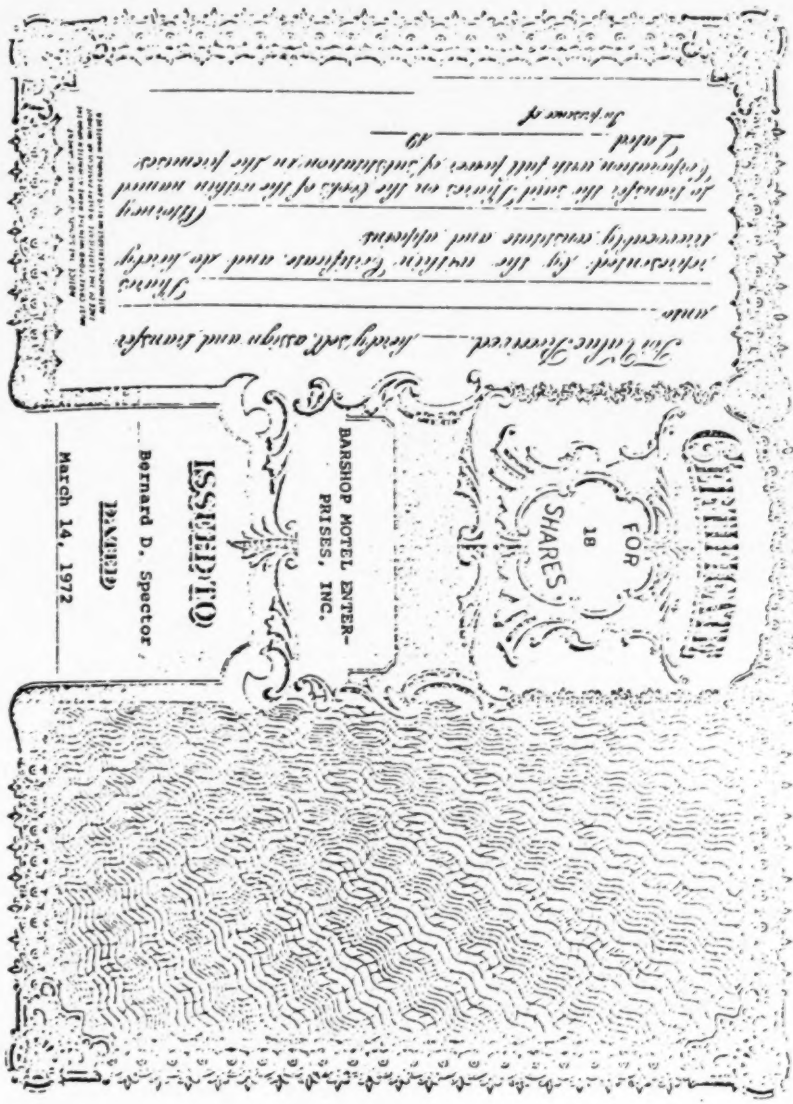
Affidavit in Reply to Opposition



ANNEX F

Stock Certificate

Stock Certificate



ANNEX G

The Constitution of the United States, Article III, Section 2, provides:

The judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, the Laws of the United States, and Treaties made, or which shall be made, under their Authority; . . .

* * * *

The pertinent provisions of the Securities Exchange Act, 15 U.S.C. § 78a, *et seq.*, provide as follows:

§ 78c. *Definitions and application — Definitions*

* * * *

(13) The terms "buy" and "purchase" each include any contract to buy, purchase, or otherwise acquire.

(14) The terms "sale" and "sell" each include any contract to sell or otherwise dispose of.

* * * *

§ 78j. *Manipulative and deceptive devices*

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange —

* * * *

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

* * * *

§ 78aa. *Jurisdiction of offenses and suits*

The district courts of the United States, and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this chapter or the rules and regulations thereunder. . . .

Statutes and Rules Involved

Exchange Act Rule 10b-5, 17 C.F.R. § 240.10b-5 provides:

Employment of Manipulative and Deceptive Devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

The pertinent provisions of Rule 8 of the Federal Rules of Civil Procedure provide as follows:

General Rules of Pleading

(a) *Claim for Relief.* A pleading which sets forth a claim for relief, whether an original

claim, counterclaim, cross-claim, or third-party claim, shall contain (1) a short and plain statement of the grounds upon which the court's jurisdiction depends, . . .

* * * *

(f) *Construction of Pleadings.* All pleadings shall be so construed as to do substantial justice.

The pertinent provisions of Rule 12 of the Federal Rules of Civil Procedure provide as follows:

Defenses and Objections — When and How Presented — By Pleading or Motion — Motion For Judgment on the Pleadings

* * * *

(b) *How Presented.* Every defense, in law or fact, to a claim for relief in any pleading, whether a claim, counterclaim, cross-claim, or third-party claim, shall be asserted in the responsive pleading thereto if one is required, except that the following defenses may at the option of the pleader be made by motion: (1) lack of jurisdiction over the subject matter, . . . (6) failure to state a claim upon which relief can be granted, . . . A motion making any of these defenses shall be made before pleading if a further pleading is permitted. No defense or objection is waived by being joined

with one or more other defenses or objections in a responsive pleading or motion. If a pleading sets forth a claim for the relief to which the adverse party is not required to serve a responsive pleading, he may assert at the trial any defense in law or fact to that claim for relief. If, on a motion asserting the defense numbered (6) to dismiss for failure of the pleading to state a claim upon which relief can be granted, matters outside the pleading are presented to and not excluded by the court, the motion shall be treated as one for summary judgment and disposed of as provided in Rule 56, and all parties shall be given reasonable opportunity to present all material made pertinent to such a motion by Rule 56.

* * * *

The pertinent provisions of Rule 56 of the Federal Rules of Civil Procedure are as follows:

Summary Judgment

* * * *

(b) *For Defending Party.* A party against whom a claim, counterclaim, or cross-claim is asserted or a declaratory judgment is sought may, at any time, move with or without supporting affidavits for a summary judgment in his favor as to all or any part thereof.

(c) *Motion and Proceedings Thereon.* The motion shall be served at least 10 days before the time fixed for the hearing. The adverse party prior to the day of hearing may serve opposing affidavits. The judgment sought shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.

* * * *

(e) *Form of Affidavits; Further Testimony; Defense Required.* Supporting and opposing affidavits shall be made on personal knowledge, shall set forth such facts as would be admissible in evidence, and shall show affirmatively that the affiant is competent to testify to the matters stated therein. Sworn or certified copies of all papers or parts thereof referred to in an affidavit shall be attached thereto or served therewith. The court may permit affidavits to be supplemented or opposed by depositions, answers to interrogatories, or further affidavits. When a motion for summary judgment is made and supported as provided in this rule, an adverse party may not rest upon the mere allegations or denials of his pleading, but his response, by affidavits or as otherwise provided in this rule, must set forth specific facts showing that there is a genuine issue for trial. If he does not so respond, summary judgment, if appropriate, shall be entered against him.

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